9 Conclusions

The reference and the monopoly situations

9.1. Under the reference dated 7 May 1993, made under sections 47(1), 49(2), 49(3) and 50(1) of the Fair Trading Act 1973 (`the Act')-see Appendix 1.1, we are required to investigate and report on whether a monopoly situation exists in relation to the supply in the United Kingdom otherwise than by retail sale of ice cream intended for immediate consumption; and, if so, by virtue of which provision of sections 6 to 8 of the Act that monopoly situation is to be taken to exist; and in favour of what person or persons that monopoly situation exists. We are also required to examine whether any action or omission on the part of that person or those persons in respect of the supply to retailers of refrigerated cabinets on terms which prevent the retailer from using the cabinet to stock for sale ice cream supplied by other suppliers-a practice commonly referred to as `freezer exclusivity'-operates or may be expected to operate against the public interest.

9.2. `Ice cream' is defined in the terms of reference to include water ices, ice lollies, frozen yoghurt and ice cream to which substances such as fruit and chocolate have been added, but does not include soft mix ice cream. Ice cream intended for immediate consumption is generally referred to as `impulse' ice cream; this term is sometimes used to include soft mix ice cream as well as the reference products although, as explained in paragraph 9.7, we have regarded `impulse' ice cream for the purposes of this report as synonymous with the reference products. As shown in Table 3.1, Birds Eye Wall's Ltd (BEW)-a subsidiary of Unilever PLC-accounted for about two-thirds of sales by value of wrapped impulse products in the UK in 1992; its share of the total reference products (wrapped impulse products plus scoop ice cream but excluding soft mix) was somewhat less, but nonetheless above 50 per cent. We have, therefore, concluded that a monopoly situation exists in the supply of impulse ice cream by virtue of section 6(1)*(a)* of the Act (a `scale monopoly' situation). We further conclude that the monopoly situation we have identified exists in favour of BEW.

9.3. We also considered whether a complex monopoly situation exists as defined in section 6(1)*(c)* of the Act, ie whether at least one-quarter of the goods specified in the terms of reference are supplied by two or more persons who voluntarily or not, or by agreement or not, so conduct their respective affairs as in any way to prevent, restrict or distort competition in connection with the production or supply of those goods. As was apparent in Table 3.1, the three largest suppliers of wrapped impulse ice cream are BEW, Nestlé UK Ltd (Nestlé-now the owner of Lyons Maid) and Mars UK Ltd (Mars), together accounting in 1992 for about 88 per cent of sales of wrapped impulse ice cream and slightly less of the reference products as a whole. Both BEW and Nestlé supply exclusive cabinets; Mars supplies cabinets on terms which require the stocking of a full range of Mars products and which, although not explicitly preventing other suppliers' products being stocked, have a similar effect given the size of most of Mars' cabinets. In our view, therefore, BEW, Nestlé and Mars are members of a group which supplies at least one-quarter of the reference products in the UK, and which conduct their affairs so as to restrict competition in the supply of impulse ice cream, in that they supply to retailers refrigerated cabinets on terms which prevent the retailer from using the cabinet to stock for sale ice cream available from other suppliers. We conclude that a complex monopoly situation exists by virtue of section 6(1)*(c)* of the Act, and that this complex monopoly situation exists in favour of BEW, Nestlé and Mars. Neither this conclusion nor that relating to the scale monopoly in itself implies the existence of any facts which operate or may be expected to operate against the public interest.

9.4. As is clear from Chapters 3 and 7, there are a large number of other suppliers of impulse ice cream-perhaps as many as 1,000-in the UK. We received information from about 50 such suppliers, about a quarter of whom acknowledged that they supplied cabinets on an exclusive basis. Taking into account, however, the much smaller market share of such other suppliers, we decided that it was inappropriate to include them as members of the complex monopoly group. It may be noted that, in a number of cases, the terms on which freezers are supplied rest on informal understandings rather than on written contracts and that even where exclusivity is formally claimed, both the intention and the capacity to enforce it are widely variable. Some manufacturers think it worth supplying a cabinet if it results in a reasonable level of sales of their products, and do not exert themselves to expel intruders so long as those sales do not fall below what they regard as a tolerable level.

9.5. We have therefore to examine whether any action or omission in respect of freezer exclusivity on the part of BEW as a scale monopolist or on the part of BEW, Nestlé or Mars as members of a complex monopoly group operates or may be expected to operate against the public interest.

The market for impulse ice cream

9.6. The size of the total UK ice cream market in 1992 has been estimated at some £785 million at retail prices including VAT. Sales of the reference products are estimated at some £275 million, and soft mix accounts for a further £55 million. Of the reference products, sales of wrapped impulse are estimated at some £233 million, and sale of scoop ice cream at some £42 million. Other than the reference products and soft mix, ice cream is sold in multi-packs-supermarket sales of products otherwise classified as impulse but sold for subsequent consumption-and in the form of other take-home products, such as ice cream sold in blocks, to be served in individual portions at home.

9.7. As discussed in paragraphs 3.3 to 3.6, the distinction between `impulse' and `take-home' ice cream is not rigid, although the nature of the purchase is somewhat different as are the outlets at which they are generally sold, and the products serve somewhat different needs: hence also the considerably higher price for impulse than for take-home products. Similarly, there is a degree of overlap in some circumstances between soft mix and impulse products as defined in the terms of reference, although many of the outlets selling wrapped impulse products do not sell soft mix, which requires a separate machine to be staffed at the point of sale. We acknowledge that scoop ice cream (included in the reference products) also differs in some aspects from wrapped impulse products, often being sold in different outlets, or from different cabinets, but this does not significantly affect our analysis. We therefore regard impulse ice cream, as defined in the terms of reference, as a sensible market in the context of the current investigation: it also distinguishes those ice cream products, sold from freezers, in which the issue of freezer exclusivity has arisen.

9.8. Wrapped impulse products have themselves been subdivided into a number of categories appealing to different sectors of the market: for example, chocolate bars aimed somewhat more at adult consumers, filled cones, refreshment (including water ices) and lines presented specially for children.

9.9. A further distinctive feature of the impulse sector is that it continues to be served by leading branded products, the development of own brands being barely evident in the case of wrapped impulse products. (Supermarket groups have developed their own brands of multi-packs but these are not part of the impulse market.) The importance of branded products is reflected in the substantial advertising expenditure particularly of some new entrants to the market, in one case of over 20 per cent of turnover.

The MMC's 1979 report

9.10. The MMC reported on ice cream and water ices in 1979.[1] It found a number of practices to be against the public interest, including:

(a) A requirement as a condition of supplying reference goods to a retail outlet that the reference goods of other suppliers should not be stocked-`outlet exclusivity'. The MMC recommended that this practice should end, which took effect as part of a number of undertakings given by the main suppliers of ice cream to the Secretary of State (see Appendix 3.1).

(b) Provision of a refrigerated cabinet on terms which prevent the customer (in general the retailer) from using it to stock reference goods of other suppliers when the supplier providing the cabinet cannot meet the customer's requirements. The MMC recommended express provisions permitting the

[1] *Ice Cream and Water Ices: a Report on the Supply in the United Kingdom of Ice Cream and Water Ices*, Cmnd 7632, August 1979.

customer to stock and sell reference goods of other suppliers when the supplier himself cannot meet the customer's requirements. This provision is now incorporated in contracts of the main companies for supply of refrigerated cabinets. Otherwise the MMC acknowledged that provision of exclusive cabinets excluded other suppliers from a retail outlet too small to be expected to sell from more than one cabinet. The MMC did not, however, find freezer exclusivity *per se* to be against the public interest. Their report noted the argument that `if cabinets were no longer provided the number of outlets, particularly those of smaller retailers, selling reference goods might fall significantly. This would reduce the scope for competition in the retail market, the opportunities for entry to the market or for increased sales on the part of the smaller suppliers, and limit consumer choice'. The MMC did, however, express the hope that the two main suppliers at that time-BEW and Glacier Foods Ltd (Glacier), predominantly owned by Lyons Ice Cream Holdings Ltd-would in the longer term make it easier for customers to buy their own cabinets.

(c) Various practices by Glacier, eg the requirement that wholesalers of Glacier products should not sell the reference goods of other suppliers; that customers buying soft ice cream mix from Glacier should also take Glacier's supplies of hard ice cream; that Glacier's franchisees should only stock or sell specified brands. The MMC recommended that these requirements should cease, as was done.

(d) The period of BEW's and Glacier's agreements, which the MMC recommended should be of no more than 12 months' duration, and arrangements for payment of retrospective bonuses: these practices were subsequently amended, in the sense the MMC proposed, though with some changes to the detailed recommendations.

9.11. During the present inquiry, we did, however, become aware of a number of cases in which landlords (including some local authorities) sought tenders for sale of impulse ice cream on an exclusive basis. The extent and effect of such `elective exclusivity' is not directly relevant to our inquiry, given our restricted terms of reference. We also found evidence of a number of agreements between BEW and retailers which, at the request of the retailers, were longer than the one-year period stipulated in the undertakings following our earlier report. These were regarded by BEW as within the spirit if not the letter of the undertakings, but again were not of direct relevance to the issue of freezer exclusivity *per se*.

Recent market developments

9.12. There have been a number of significant changes in the structure of the market since our previous report. BEW estimates that in 1979 BEW and Lyons Maid each had about 45 per cent of the impulse market. BEW's share of the wrapped impulse market has subsequently increased to about two-thirds, that of the Lyons Maid brands has slumped to only about 10 per cent. The decline of Lyons Maid is discussed in more detail in Chapter 3: the business went through two changes of ownership before the main brands were recently acquired by Nestlé, and many in the industry regard it as having failed to invest adequately and compete effectively in the 1980s.

9.13. There have also been a number of new competitors in the market, notably Mars. Mars estimated its share of the wrapped impulse market in 1992 at about 16 per cent: but it suggested that in the summer of 1993 it had a higher share, some 20 per cent, in that sector of the market-chocolate bars-where it has mainly chosen to compete, with a share of some 30 per cent of chocolate bars outside the leisure sector where it has found distribution to be particularly difficult. Mars' entry to the market was based on established confectionery brands, and supported by significant advertising expenditure. Mars told us, however, that when it first entered the market with one product, it had assumed it would be able to secure distribution from existing freezer cabinets in retail outlets: when it found that this was often impossible, it provided its own cabinets to secure retail distribution. Other recent entrants include Treats Ice Cream Ltd (Treats) (formerly owned by BEW, now an independent company following a management buy-out), Häagen-Dazs UK Ltd (Häagen-Dazs) (a subsidiary of Grand Metropolitan PLC) and Schöller Ice Cream Ltd (the subsidiary of a major supplier of ice cream elsewhere in the EC).

9.14. A number of parties referred to Mars' entry to the market as providing an additional stimulus to product innovation. Mars' products, based on well-known confectionery brand names, incorporated a higher quality both of ice cream and chocolate. Its entry appears to have stimulated a demand for `chocolate-bar' products, particularly among adults, of a quality and price higher than previously prevailed in the market: following Mars' entry, the quality and price of a number of existing BEW brands were also increased (see Table 3.9). BEW, on the other hand, argued that it had itself introduced a succession of new products irrespective of competition from Mars.

Profitability

9.15. As shown in Chapter 2, there is no evidence of excess profitability on sales of impulse ice cream. BEW's return on net assets-which averaged about 15 per cent over the last four years-is somewhat below that for the economy generally over that period.[1] The financial performance of some other main suppliers is significantly poorer than that of BEW, although we received no indication that they would have to consider withdrawing from the market.

Distribution

9.16. As discussed in Chapter 3, ice cream must be kept at a low temperature at all stages of production and distribution, from the factory to the point of retail sale. To supply the retail market, manufacturers need their own distribution network, including cold stores and refrigerated vehicles, or access to a distributor with such facilities.

9.17. Almost all parties from whom we heard agreed that distribution is a key aspect of competition given the nature of the product, with demand highly sensitive to weather and rapid delivery required to cope with unpredictable peaks of demand given the typical retailer's limited facility for holding stocks. It was suggested to us that specialist distributors were better able to respond to such demand. It was also agreed that there were important economies of scale in distribution due, for example, to the high costs of temperature-controlled storage and transportation, and the low unit value of the products: one estimate was that a 10 per cent increase in quantity delivered could reduce unit distribution costs-which account in some cases for over 20 per cent of total cost-by as much as 10 per cent in the long term.

9.18. BEW currently distributes almost two-thirds of its impulse products through 38 exclusive concessionaires. These concessionaires cover the entire UK except the area within the M25, accounting for about 11 per cent of BEW's sales, where BEW distributes its products direct from its own cold storage depot. Its remaining sales are distributed through Wall's Whippy franchisees, through general wholesalers (although it refuses to supply regional or local wholesalers), and to a few accounts which have negotiated direct delivery.

9.19. BEW's current distribution arrangements have evolved from the in-house distribution system used at the time of our previous report, its concessionaires often acting as marketing agents for BEW, as well as distributors. It told us that it would keep its current arrangements under review, taking into account the relative performance of its concessionaires and its in-house distribution system used within the M25 area.

9.20. A number of other suppliers claimed that BEW's exclusive concessionaire system put it at a significant advantage: given, for example, economies of scale, any competing distribution system would be unable to provide as good a service to retailers, and would incur higher unit costs. BEW's current arrangements would appear to have some similarities to those of Glacier, on which we commented in our previous report, but it is only open to us to consider these arrangements in so far as they relate to the issue of freezer exclusivity. We return to this point in paragraph 9.56.

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[1]MMC analysis of Extel Micro-EXSTAT database of some 600 manufacturing company accounts gives return on capital employed (trading assets) of 20.4 per cent in 1989, 18.9 per cent in 1990, 14.9 per cent in 1991 and 13.0 per cent in 1992-an average of 16.8 per cent. The average for all companies in the database, including non-manufacturing, was some 16.3 per cent over the four years.

Freezer exclusivity

9.21. The retail sale of impulse ice cream requires a freezer cabinet to ensure the quality of the product. The supply of freezer cabinets to retailers has been one means of promoting retail sales of impulse ice cream.

9.22. BEW and Nestlé currently supply freezers `free' (ie not separately charged for) on loan on condition that they are not used to stock competing products unless their products are temporarily unavailable. Nestlé, however, distributes certain Mars products which do not directly compete with its own range and which can be stocked in Nestlé cabinets. Mars initially sold freezers to retailers, but with an equivalent value of Mars ice cream supplied free: more recently, it has supplied freezers free-on-loan subject only to the requirement to stock the full Mars range.

9.23. Of other suppliers, Treats sells freezers with vouchers permitting the cost of the freezer to be recovered by purchase of its products. Häagen-Dazs supplies freezers on exclusive terms and with fittings designed for Häagen-Dazs products. About a quarter of other manufacturers from which we heard acknowledged that they insisted on exclusivity, but some others requested it, or aimed to secure a good representation of their products in the cabinet, or stipulated a minimum percentage of space to be used for stocking their products. One supplier offered retailers the choice of a `free' cabinet on an exclusive basis, or a `hired' one on a non-exclusive basis. Those suppliers of impulse ice cream who did not supply freezers generally felt themselves to be at a disadvantage. We are also aware of wholesalers who supply or facilitate the supply of freezers to retailers sometimes on condition that they provide the stock, which may come from several manufacturers.

9.24. At the time of our previous report, comprehensive evidence was not available on the extent to which ice cream was sold from exclusive cabinets: information in the report suggested, however, that some 15 to 20 per cent of retailers then had their own freezers, the remainder being subject to both freezer and, in many cases, outlet exclusivity. We received varying evidence on the extent of freezer exclusivity during the current inquiry (see paragraphs 3.64, 4.59 and 6.21 and Appendix 3.2).

9.25. BEW estimated, as summarized in paragraph 3.64, that there are some 90,000 general trade outlets (excluding, for example, multiple grocery outlets) selling wrapped impulse ice cream, some 63,000 of which stock BEW ice cream. It also estimated that about one-third of outlets-some 32,000-have one or more BEW freezers but no other cabinets; while some 30,000 outlets-also about one-third of the total-currently have their own cabinets: similar to the proportions from a much larger survey of 46,000 outlets conducted for Nestlé.

9.26. We ourselves commissioned a survey of some 1,500 retail outlets-see Appendix 3.2. The survey did not give a fully representative sample of retail outlets, excluding multiple confectionery/tobacconist/newsagent outlets (CTNs) from whom we received evidence direct (most of whom have cabinets provided by more than one ice cream supplier, and sell more than one supplier's products in many of their outlets) and leisure outlets, where Mars has had more difficulty competing: it did, however, supplement other evidence as to the extent of freezer exclusivity and provided a sample of the views of independent retailers.

9.27. BEW remains in our survey the most widely available brand, being stocked in some 80 per cent of outlets compared with nearly 50 per cent for Mars. These were similar to the figures in the Nestlé survey, and one survey carried out for BEW (although BEW subsequently argued that Mars' availability was understated and could be as much as 73 per cent of outlets, weighted by turnover). All the surveys we saw showed that about one-quarter of outlets sold Nestlé brands.

9.28. About 36 per cent of respondents to our survey had only one front freezer for exclusive use and no other, but a similar proportion of respondents did not have a manufacturer-owned freezer at all. (Much the same picture emerges from the Nestlé survey.) About one-quarter of outlets had more than one freezer: the Nestlé survey gave a somewhat lower figure. The Nestlé survey and our own also showed that at least one-half of outlets sold more than one manufacturer's products.

9.29. On the figures available to us, therefore, freezer exclusivity appears to pose less of a restriction in supply of impulse ice cream than at the time of our previous report. This itself is to a large extent explained by the investment made by Mars in installing second freezers in retail outlets, and the decision of retailers themselves to install a second manufacturer's freezer, or their own.

9.30. A number of parties from whom we heard argued that many retail outlets did not have `space' for a second freezer. The availability of space cannot be regarded as purely a physical constraint, but as shorthand for the perceived opportunity cost compared to other uses of any sales area. About 34 per cent of respondents to one BEW survey had a single freezer and stated that they would not have space to install a second, or two smaller freezers. On the other hand, BEW estimated that only some 12 per cent of its sales were to outlets with BEW exclusive freezers and unable to install a second freezer. About one-quarter of respondents to our survey had only an exclusive freezer and said that lack of space was the reason for not getting a second freezer; but the figure is reduced to less than one-fifth after allowing for those who said that they would consider installing two smaller freezers instead of the present larger one. The survey results also showed that these are predominantly smaller or medium-sized outlets, accounting for a somewhat lower proportion of sales.

9.31. The variety of information we have seen shows the extent of choice available to retailers as to the products to be stocked, and the means to be used for stocking them. Retail outlets with space for only one freezer and unwilling to substitute two smaller freezers for the existing freezer-no more than one-third of outlets on the information we have seen and possibly a lot fewer-have the option to install one exclusive freezer supplied by a manufacturer, or to install their own freezer free of any restriction: an increasing proportion of outlets do so in order also to stock other frozen products. Even if they should choose a manufacturer's freezer, they are initially obliged to maintain that freezer in place for no more than a year, and subsequently are able to switch at much shorter notice. Other retail outlets-the majority on the figures we have seen-can also consider installing a second manufacturer's freezer, or their own freezer additional to one supplied by a manufacturer. We were told of one market research study indicating that a second freezer would increase sales: some other research showed that a larger `industry freezer' free of restrictions would produce better sales than two smaller freezers although subsequent experience casts doubt on this. Retailers themselves are clearly in a position to make their own judgment, as some of the multiple CTN chains, experimenting in the use of industry freezers, are attempting to do.

Charges for use of exclusive freezers

9.32. Unlike practice in some other EC countries (the Republic of Ireland, for example) both BEW and Nestlé generally charge, in their standard terms, lower prices for supply of ice cream (by means of a higher retrospective bonus) for retailers without exclusive freezers. As shown in Table 2.7, BEW has no bonuses for outlets with gross sales value (GSV) of purchases from BEW of below £800; above that amount there is a differential bonus of 6 per cent for outlets with gross sales value of between £800 and £1,070, declining to 2 per cent for outlets with GSV above £4,610. (Multiples, large buyers etc will generally negotiate terms; BEW told us that there was no inducement to take BEW rather than industry freezers, as evidenced by the number of such customers that had chosen to buy their own, and we see no reason why multiples or similar buyers should not be able to obtain better terms if they install their own freezer reflecting the cost saving to BEW.) Nestlé's bonus system is applied only to retailers with purchases of at least £1,000 in a year: the differential bonus varies between 5 per cent on the first £795 of turnover at trade list price and 2.5 per cent on turnover in excess of £4,916. Mars, on the other hand, does not distinguish in its charges between retailers with and without its cabinets.

9.33. BEW acknowledged that there was no systematic basis to its differential bonuses, but argued that the differential in terms broadly covered the cost to BEW of supplying freezers. On the figures supplied to us by BEW (see Table 2.8), it is clear that the lower bonuses on sales of impulse ice cream (in effect, the higher prices) to retailers with exclusive cabinets in many cases fall short of the cost to BEW of supplying exclusive cabinets, but the shortfall is significant mainly at lower GSVs where no bonus of any kind is paid. The annual cost to BEW of supplying a 1-metre freezer (the most common size), for example, is estimated at about £61. The higher charges (in the form of lower bonus) to retailers with an exclusive 1 metre freezer vary from zero at sales of £750, to £60, broadly equivalent to the cabinet cost, at £1,000 annual sales. For a 1.5 metre cabinet (the second most common size) the annual cost to BEW of about £69 compares with higher charges for use of an exclusive cabinet varying between £43.75 (below cost) on £1,250 sales and £100 (above cost) on £2,500 sales. There is a similar relationship between Nestlé's differential charges and its freezer costs. We have also noted that the amount of BEW's and Nestlé's charges for the use of a freezer can only be estimated at the time the cabinet is installed, since they reflect the difference between the two scales of retrospective bonuses (if any), depending on the level of sales actually achieved which is not known until the end of the year. The charges will therefore be affected both by the sliding scale nature of the bonus system, being based on the percentage of GSV, and by the variation in terms according to the size band in which sales to a retailer fall. We return to these points in paragraph 9.60.

9.34. BEW's calculations also showed a more significant net benefit to a retailer of having an exclusive cabinet rather than purchasing his own (see paragraph 2.38), but in our view this comparison is less relevant. It reflects BEW's belief that it can acquire freezers at lower cost than retailers themselves due to its greater bargaining power. We see no reason why the benefits of BEW's bargaining power should not be passed on to its users in this way, although we are doubtful that retailers would necessarily have to acquire freezers on terms as unfavourable as BEW suggests. Retailers already have a wide degree of choice in acquiring freezers: they can, for example, purchase from impulse ice cream suppliers who offer freezers with an equivalent value of `free product'. We are also not aware of any distortion in the market sufficient to prevent the development of further competition in supply of freezers, on terms as favourable as those available to BEW. Retailers' overall turnover may also benefit if they sell a greater product range, which is not allowed for in BEW's calculations.

The public interest

9.35. Concern about freezer exclusivity relates primarily to its imposition by BEW as the scale monopolist, although we have also considered the imposition of freezer exclusivity by BEW, Nestlé and Mars as members of the complex monopoly group identified in paragraph 9.3. Freezer exclusivity has moreover to be considered as it is at present applied and in the current circumstances of the impulse ice cream market in the UK. We are aware of an appeal by Mars to the Irish Supreme Court against a recent ruling of the Irish High Court upholding exclusivity and of other related proceedings by the European Commission (see Appendix 5.1): while we recognize that the eventual ruling of the European Commission may have implications for member states generally, including the UK, we have to consider the issue of exclusivity on its merits and solely in the circumstances of the UK market and in the context of domestic legislation.

9.36. As is apparent in Chapters 4 to 8, we received a wide range of views on the effects of freezer exclusivity. A majority of suppliers from whom we heard argued that the practice was against the public interest, inhibiting competition and entry, and adversely affecting consumer choice, innovation and price.

9.37. As well as BEW, Nestlé argued strongly in favour of freezer exclusivity, the retention of which it regarded as necessary if Lyons Maid was to recover market share and compete on equal terms with BEW given BEW's other competitive advantages, in particular in distribution. Nestlé further argued that the removal of freezer exclusivity would enhance BEW's market share, a point accepted in part by BEW. Smaller suppliers on balance argued against exclusivity even when they themselves practise it partly in response to BEW, although some were not opposed and one suggested that, following the example of some multiple CTNs, freezer exclusivity might be abandoned over time anyway, as retailers increasingly chose to install their own cabinets.

9.38. There was a range of views from retailers, our own survey showing at the most a very slight balance against the practice, although some individual retailers from whom we heard were clearly irritated with the methods used to enforce exclusivity. Our survey did, however, show widespread satisfaction with BEW's delivery and maintenance arrangements, as with that of other suppliers. Noticeable also, however, from our retailers survey was the limited extent to which retailers told us that they were asked for products they did not stock. We received very little evidence direct from consumers, although the Consumers' Association argued against the practice.

9.39. In our previous report we referred to the argument that freezer exclusivity increased the number of outlets offering ice cream: similar arguments were put forward during the current inquiry. To sell ice cream, a retailer needs a freezer cabinet, and a supplier of ice cream must persuade the retailer both to make space for the cabinet and to find some means of financing its capital and maintenance costs. If the retailer is unable or unwilling to finance the cabinet himself, the supplier may provide the retailer with a cabinet, but if he does so the supplier will expect to achieve a return on his capital investment. Ice cream suppliers have done this by demanding that only their products will be sold from their cabinet, so that they are guaranteed sales from the cabinets they supply: in this way, it was argued, by supplying free-on-loan exclusive freezers, the two main suppliers, BEW and Lyons Maid, have developed the market for impulse ice cream, to the benefit of retailers and consumers.

9.40. It was suggested that without freezer exclusivity suppliers could not be expected to provide freezers on their current terms. Since charges for use of freezer cabinets were based on turnover, loss of sales from a cabinet would lead to an under-recovery of freezer costs, while competitors would have free access to cabinets, and be in a position to secure retail distribution without contributing to freezer costs. The present differential charges, based on sales, would need to increase; or cabinets would have to be rented or sold to retailers at a price more closely related to cost: as shown also in paragraph 9.33, this could result in a significant increase in charges for retailers with a lower volume of sales.

9.41. It was again argued that this would result in a reduction in the number of outlets selling ice cream, but we received conflicting evidence on the point. Only 3 per cent of retailers responding to the MMC survey said that, if current arrangements changed, they would expect to stop selling impulse ice cream, suggesting that the market may now be at the stage where abandonment of freezer exclusivity would have only a limited impact on availability of impulse ice cream. A survey by BEW suggested that between 12 and 20 per cent of retailers would stop stocking impulse ice cream, although the higher figures may reflect a rather high estimate in the question put to retailers of the costs associated with buying or renting a freezer. Even if the results of our survey were correct on this point, BEW's investment in developing the market should not, in our view, be put at risk, nor should any future such investment by BEW or other suppliers be deterred, unless there were clear evidence that freezer exclusivity now operated against the public interest.

9.42. In considering effects adverse to the public interest, we initially identified eight issues which we put to BEW, Mars and Nestlé:

(a) Whether consumers would benefit from:

(i) greater choice;

(ii) keener price competition,

if retailers were free to stock competing products in what would often be the one freezer cabinet for which there was room on their premises.

(b) Whether the present arrangements prevent other manufacturers from entering the impulse ice cream market or raise the cost of entry or adversely affect the profitability of BEW's competitors, thereby further damaging competition.

(c) Whether there has been an adverse effect on competition at the wholesale level.

(d) Whether freezer exclusivity is not in some circumstances tantamount to outlet exclusivity.

(e) Whether freezer exclusivity may diminish incentives to innovation (eg in introduction of new products) and greater efficiency.

(f) Whether the terms on which ice cream is supplied to retailers with/without exclusive cabinets distort retailers' choice between using exclusive freezers or acquiring their own freezers.

(g) Whether aspects of the distribution system may be regarded as reinforcing the effects of freezer exclusivity and are likely to require attention if any remedies are to be effective. These aspects are (i) refusal by BEW to supply, in the case of regional wholesalers, and (ii) exclusive supply-the obligation on retailers with BEW's cabinets to buy only from a concessionaire, and on concessionaires not to handle competitors' products.

(h) Whether freezer exclusivity itself has the adverse effect of allowing the maintenance of exclusive distribution arrangements, which may be both uneconomic, and detrimental to competition.

Effect on competition

9.43. Recent developments in the market, to which we referred in paragraphs 9.12 to 9.14, themselves suggest that competition has been effective, irrespective of freezer exclusivity. Poor performance by Lyons Maid-in particular the failure to develop its brands and difficulties in both production and distribution-resulted in a dramatic reduction in its market share notwithstanding its insistence on freezer exclusivity. BEW, on the other hand, has maintained and increased its market share not only due to any advantages that may arise from its installed base of exclusive freezers, but by developing its brands and competing effectively on price, product range and the efficiency of its delivery arrangements to replace Lyons Maid in a large number of outlets. Conversely, BEW can only retain its existing position if it continues to compete effectively. Hence, the experience respectively of Lyons Maid and BEW demonstrates in our view that, notwithstanding the advantages of freezer exclusivity, market share has to be won or sustained by effective competition in other ways, particularly given recent entry to the market.

9.44. The main new entrant-Mars-has built up a share of the overall market of over 10 per cent, but a significantly higher share-some 20 to 30 per cent-of that sector of the market (chocolate bars) where it has chosen to concentrate, and its products are available in about one-half or more of retail outlets. Lyons Maid itself now offers the prospect of much improved competition under the new ownership of Nestlé, which it believes it can only sustain if freezer exclusivity is maintained. Other entrants to the market have established a significant presence.

9.45. Although some impulse ice cream prices have increased faster than inflation (see Table 3.9), this would appear to reflect, given the wide choice of products available, a consumer preference for high-quality, higher-priced product. The evidence of at most modest profitability, to which we referred in paragraph 9.15, would not suggest that prices are above competitive levels, a point to which we return in paragraph 9.55.

9.46. Given recent market developments, freezer exclusivity can be regarded as adversely affecting competition (the issue in paragraph 9.42*(a)*(ii)) only in a narrow sense. A retailer with an exclusive cabinet can clearly not stock competing products in that cabinet, hence in one-half or less of outlets there is no competition to supply the consumer at the point of sale. As we have noted, however, there are many options open to the retailer. In the majority of outlets, he can choose to install a second manufacturer's cabinet, or his own freezer. Even in smaller outlets, there is active competition to supply the single freezer, and retailers have the choice of installing their own freezer.

9.47. In this context, we also considered the argument that freezer exclusivity may be regarded as tantamount to outlet exclusivity (the issue in paragraph 9.42*(d)*). As we indicate above, the proportion of outlets with one exclusive cabinet, and without the space to install a second freezer or the inclination to install two smaller freezers in place of the manufacturer's freezer, appears to be limited to at most a third of all outlets and possibly a lot fewer. Even in these outlets, retailers can choose to install their own cabinets, free of any exclusivity. Any resulting outlet exclusivity is, therefore, a matter of informed choice on the part of the retailer-`elective' rather than dictated by BEW or any other suppliers.

9.48. We considered, on the other hand, whether recent developments may present too optimistic a view of the market and whether freezer exclusivity could not inhibit competition in the longer term by raising entry costs (the issue in paragraph 9.42*(b)*). The extent of competition currently owes much to Mars' own efforts to install freezers, at considerable expense, as well as to its marketing and product innovation. Its success in establishing its current market share shows that freezer exclusivity is less a barrier to entry than a cost of entry, no different in its effects to other costs such as advertising. Mars is still incurring [*] losses, but there is no evidence that it is reconsidering its presence in the market, and it is too soon in our view to suggest that its financial position shows any fundamental weakness as a result of freezer exclusivity.

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*Detail omitted. See note on page iv.

9.49. A number of smaller manufacturers have also, through supplying exclusive freezers, been able to establish strong regional or local positions or concentrated on certain sectors of the market, such as cinemas: the supply of exclusive freezers-although in part a defensive move-is one means of competing against heavily advertised national brands. Other manufacturers have been able to establish a limited presence in the market without supplying exclusive freezers. It is indeed unclear to us whether the wider use by retailers of non-exclusive freezers would necessarily benefit the smaller, regional manufacturers. Fewer than 10 per cent of retailers responding to our survey said that they would increase the range of products stocked were freezer exclusivity to be ended. A number of multiple CTNs to whom we spoke who have installed their own freezers stock products of only the three main suppliers. Smaller manufacturers could still be disadvantaged, therefore, by the brand strength and distribution arrangements of the major suppliers.

9.50. We considered the further argument that freezer exclusivity required a supplier to provide a full range of products, the more so if he was to replace an existing supplier's sole cabinet in any retail outlet. Mars' success partly results from its current agreement for Nestlé to distribute certain of its products, and for these products to be stocked in Nestlé's cabinets. Given the strength of the Mars brands, such an arrangement, either with Nestlé or with an alternative supplier, would seem in both parties' interests. We would be surprised if competitors to BEW proved unable to put together combinations of product ranges and freezer offers that would compete effectively with BEW.

9.51. We also noted Nestlé's argument that, without exclusive cabinets, it could not achieve the drop sizes necessary for efficient delivery of its products: hence, it may not be economic in terms of frequency and drop size to supply retailers' own freezers, unless all distributors were free to supply a wider product range. We acknowledge that, with current arrangements, freezer exclusivity may enable some of the main suppliers to maintain the drop sizes necessary to secure economies in distribution of impulse ice cream (to which we referred in paragraph 9.17) and that, in the short term, any weakening of freezer exclusivity could increase distribution costs. We would not, however, be surprised if, as some parties suggested to us, the industry continued to evolve in response to the initiatives of suppliers, and the demands of retailers and their customers to stock wider ranges of products, so reducing the extent both of freezer exclusivity and of exclusivity in distribution arrangements, and improving distribution economies; freezer exclusivity would not, in our view, prevent this happening.

Effect on consumer choice

9.52. We considered the argument, of some suppliers and the Consumers' Association, that consumer choice requires the stocking of different manufacturers' products in the same freezer, or at least the same retail outlet: and that freezer exclusivity inhibits such choice (the issue in paragraph 9.42*(a)*(i)). Despite freezer exclusivity, there is, as mentioned in paragraph 9.27, wide availability of the main brands, particularly BEW brands and to a somewhat lesser extent those of Mars. Of the main brands, availability of Nestlé brands is the most limited, but Nestlé appears determined to improve this, as long as freezer exclusivity is maintained. Other suppliers have established their products in a more limited range of outlets-specializing, for example, in health food, or video rental shops. There is therefore a wide choice of different suppliers' products available in different outlets.

9.53. Mars quoted evidence to us that, if a customer's preferred product is not stocked in a shop, most consumers will choose from the products that are available: very few will go to another shop. On the figures we have seen there is a choice of more than one manufacturer's product in at least one-half of outlets. Customers of shops with only one exclusive cabinet clearly have only the one manufacturer's products from which to select: but in our view this represents a restriction of choice also only in a very limited sense. Consumers normally still have the option of using other retail outlets, of which there will often be several nearby (generally with the main brand stocked clearly advertised in the street): that consumers may well not do so suggests that they themselves may not perceive any significant limitation on choice.

9.54. In addition, as paragraph 9.31 has explained, there are a number of alternatives open to the retailer; in reaching his decision, the retailer will himself take customer preferences into account. We are, moreover, not convinced that the uniform adoption of retailers' own cabinets would itself significantly improve choice for consumers: the range of products stocked is likely to be limited by space constraints, and retailers may still prefer mainly to stock one manufacturer's products given, for example, ease of supply and invoicing arrangements. We noted in paragraph 9.49 the limited proportion of retailers who said that they would increase the range of products stocked were freezer exclusivity to be ended.

Assessment

9.55. In our view, therefore, there is insufficient evidence to demonstrate that the imposition by BEW, Nestlé or Mars of freezer exclusivity as applied in the UK market as it is currently developing inhibits competition or consumer choice. Moreover, there is no evidence that it is adversely affecting the level of prices paid by retailers or consumers, as is also indicated by the limited profitability in the UK market. Similarly, given recent market developments, we find it difficult to argue that freezer exclusivity diminishes incentives to innovation or efficiency (the issue in paragraph 9.42*(e)*), or otherwise adversely affects consumers or the public interest. We received no evidence that BEW was in any sense inefficient: its distribution arrangements in particular, indeed, were regarded as highly efficient, hence the desire of some of its competitors that BEW concessionaires should be allowed to distribute their products. In our view, therefore, the imposition of freezer exclusivity in the UK market as it is currently developing does not operate against the public interest. This conclusion applies equally to freezer exclusivity considered as a practice of BEW as the scale monopolist, and more widely to freezer exclusivity considered as a practice of BEW, Nestlé and Mars as members of a complex monopoly group.

Effects on wholesaling and distribution

9.56. As we mentioned in paragraph 9.20, it is clear that a number of BEW's competitors were concerned about BEW's exclusive concessionaire system and its restrictions on supply to certain wholesalers. Similar concerns were expressed by the wholesalers themselves. It is not open to us to consider whether BEW's current distribution arrangements may have anti-competitive effects, other than in the context of freezer exclusivity (the issues identified in paragraph 9.42*(c)*, *(g)* and *(h)*). There is no doubt, however, that the concessionaire system is a highly efficient method of distribution for BEW, and has contributed to BEW's strong competitive position. It is a development of BEW's own previous in-house distribution system, to which BEW would be free to revert although at some cost, and against which some of BEW's competitors acknowledged they would have fewer grounds to object.

9.57. Some suppliers argued that without freezer exclusivity, guaranteeing sales in outlets with exclusive freezers, the exclusive concessionaire system could not be maintained. We are not convinced by this, particularly given the concern expressed to us that, even if freezer exclusivity were abandoned, the strength of BEW's exclusive concessionaire arrangements was such that BEW's predominant market share would not be put at risk.

9.58. Many in the industry said that retailers with BEW exclusive cabinets were required to obtain supplies solely from its concessionaires. BEW firmly denied this and told us that it had taken steps to ensure that no pressure was being brought to bear on retailers not to purchase products other than from concessionaires, although its system for paying retrospective bonuses on purchases invoiced through concessionaires does understandably provide an incentive to use the concessionaire system. Given that denial, BEW's distribution arrangements must, in our view, be regarded as an issue separate from that of freezer exclusivity and on which we cannot in this inquiry comment further: we are similarly inhibited from commenting on the restrictions imposed by BEW on the products that can be stocked by its franchisees. Given also our overall finding on freezer exclusivity, the recommendations put to us by other suppliers-notably Mars (see paragraph 5.38)-relating both to exclusive cabinets and exclusive distribution arrangements do not therefore arise.

9.59. We did, however, suggest to BEW that its standard conditions of trade (as shown in Appendix 2.4) for use of its cabinets misled retailers, and could be regarded as contributing to a widespread misapprehension, in requiring that `the customer will use the refrigeration only for the purpose of storing products supplied by the company or its distributors', unless the company or its distributors are unable to deliver. BEW told us that the term `distributors' was not intended to be confined only to concessionaires, but included other wholesalers it supplied: although concessionaires could offer better service and better terms, it accepted that it should not block other legitimate channels of trade. It, therefore, agreed to remove the above reference to distributors from its conditions (see paragraph 4.54). In the circumstances, therefore, we have not concluded that BEW's standard conditions for use of exclusive freezers operate against the public interest.

BEW's terms

9.60. In examining the effects of freezer exclusivity, we put considerable emphasis on the options available to retailers. We considered whether the terms on which exclusive freezers are supplied, particularly by BEW given its large market share as the scale monopolist, could distort retailers' choice between using exclusive freezers, and acquiring their own (the issue in paragraph 9.42*(f)*).

9.61. One concern was that these terms are insufficiently transparent. BEW told us that, not only are its terms clearly stated in its retail price list, but they have also received prominent publicity in the trade press. We would be surprised, therefore, if retailers were unaware of the higher prices they pay for impulse ice cream if the manufacturer supplies the freezer.

9.62. In reaching our conclusion that freezer exclusivity does not operate against the public interest, we were significantly influenced by the current terms on which freezers are supplied, including the limitation of the duration of contracts to no more than one year, and the differential charges particularly of BEW for supply of impulse ice cream to retailers with and without exclusive freezers. We are satisfied that these charges cover the bulk of the costs associated with supplying freezers but we considered nevertheless whether the failure particularly of BEW to reflect freezer costs fully in the prices charged for each freezer could adversely affect competition.

9.63. The shortfall between BEW's costs and charges can, however, only be regarded as significant at relatively low levels of GSV-particularly purchases by the retailer of £800 a year and below: above that amount, the shortfall rarely amounts to more than 1 or 2 per cent of GSV. On BEW's figures, sales to retail outlets with BEW cabinets and a level of turnover below £800 amount to less than 5 per cent of the total value of BEW sales of impulse ice cream-hence BEW's failure to cover freezer costs affects only a relatively small proportion of its sales.

9.64. It follows that to reflect costs in charges would imply a significant increase in charges for retailers with relatively limited sales: it would require either an annual charge (of about £61 to reflect the cost of a 1 metre freezer, for example), irrespective of the volume of turnover, or-perhaps more difficult to implement-a downward extension of the differential in the current turnover-related charge between users with and without exclusive freezers. The increase in charges for a small retailer with an exclusive freezer could be as much as some 7.5 per cent or more of GSVs, a significant element of the retailer's margin. The sector of the market that would be affected is that which is most likely to reconsider stocking ice cream. The effect of BEW's current policy may, therefore, be to promote overall sales of ice cream rather than to increase its market share at its competitors' expense. This is a strategy BEW should be free to pursue should it so choose: it may indeed be profitable for it to do so, as well as beneficial to consumers, on the basis of BEW's incremental costs.

9.65. There is insufficient evidence in our view, therefore, that BEW's charging policy operates against the public interest. We have no concern about the differential charges made by Nestlé for use of cabinets or Mars' charges for supply of ice cream which do not distinguish between retailers with and without exclusive freezers, given the more limited market share of both companies and their need to compete effectively with BEW and other suppliers.

Conclusions

9.66. We have found insufficient evidence to demonstrate that freezer exclusivity as applied in the UK market as it is currently developing inhibits competition or choice, or adversely affects prices, innovation or efficiency or other aspects of the public interest; nor have we found any aspect of the conditions on which exclusive freezers are supplied or the charges for the use of exclusive freezers to have any effects adverse to the public interest. We have therefore concluded first that the following actions on the part of BEW as a scale monopolist do not operate and may not be expected to operate against the public interest:

(a) the imposition of terms for supply of refrigerated cabinets which prevent the retailer from using the cabinet to stock for sale ice cream supplied by other suppliers (paragraph 9.55);

(b) the conditions imposed by BEW for use of exclusive cabinets (paragraph 9.59); and

(c) BEW's charges for use of exclusive cabinets (paragraph 9.65).

We have concluded secondly that the following actions of BEW, Nestlé and Mars as members of a complex monopoly group do not operate and may not be expected to operate against the public interest:

(a) the imposition of terms for supply of refrigerated cabinets which prevent the retailer from using the cabinet to stock for sale ice cream supplied by other suppliers (paragraph 9.55); and

(b) the charges made for use of exclusive cabinets (paragraph 9.65).

H H LIESNER *(Chairman)*

A FORSTER

A P L MINFORD

L PRIESTLEY

A J NIEDUSZYNSKI *(Secretary)*

14 January 1994