COMPETITION COMMISSION

Scottish Milk

A report on the supply of fresh processed milk to middle-ground retailers in Scotland

Presented to Parliament by the Secretary of State for Trade and Industry by Command of Her Majesty December 2000

Web site: **www.Competition-Commission.org.uk**

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[1]These members formed the Group which was responsible for this report under the Chairmanship of Mrs D P B Kingsmill.

Note by the Department of Trade and Industry

In accordance with section 83(3) and (3A) of the Fair Trading Act 1973, the Secretary of State has excluded from the copies of the report, as laid before Parliament and as published, certain matters, publication of which appears to the Secretary of State to be against the public interest, or which he considers would not be in the public interest to disclose and which, in his opinion, would seriously and prejudicially affect certain interests.

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

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Part I

Summary and Conclusions

1 Summary

1.1. On 3 February 2000 the Director General of Fair Trading (DGFT) referred the supply of fresh processed milk, to middle-ground retailers in Scotland, to the Competition Commission for investigation and report (under the monopoly provisions of the Fair Trading Act 1973 (the Act)). We were asked to report by 2 November. Our terms of reference are at Appendix 1.1. In this report, we use 'the Commission' to refer to the Competition Commission or the Monopolies and Mergers Commission (its predecessor) as the context requires.

1.2. Scottish farms produce around 1.2 billion litres of raw milk a year, about half of which is processed as liquid milk. Around 90 per cent of household purchases are of fresh milk, with most of the remainder being sterilized or UHT milk. The raw milk not devoted to liquid processing is used to make dairy products, such as butter or cheese, or in the manufacture of other foods.

1.3. By far the largest fresh milk processor in Scotland is Robert Wiseman Dairies PLC (Wiseman) with three plants in the Scottish Central Belt and a fourth in Aberdeen. Wiseman also has a large modern dairy in Manchester, and is building another in Droitwich. There are only three other liquid milk processors of any size in Scotland: Claymore Dairies Limited (Express/Claymore), in which Express Dairies plc (Express) has a controlling stake with a plant at Nairn; Grahams Dairies which has a plant at Bridge of Allan, near Stirling; and Scottish Milk Dairies Limited located in Hamilton.

1.4. The Scottish middle-ground retailers, which our terms of reference asked us to examine, accounted for 42 per cent of retail sales of fresh processed milk in 1999/2000. The sector is made up of four main elements: the smaller supermarket chains; the convenience store chains; the symbol groups, substantially composed of separately-owned stores which come together to centralize buying and marketing; and individually-owned stores and corner shops. The supply of milk to the six larger supermarkets and their subsidiaries, and to retailers whose business is solely doorstep delivery was excluded from our inquiry.

1.5. The inquiry was triggered by a complaint to the DGFT about the behaviour of Wiseman, Scotland's largest processor, and a major rival to Express in the supply of fresh processed milk in northern England and the Midlands.

1.6. In our analysis of the market we looked at two elements: the product market and the geographic market. On the product, we concluded that the market for the supply of fresh processed milk was distinct from that for other types of liquid milk and dairy foods.

1.7. On the geographic market, we examined six issues:

(a) the extent to which there were—and had been—price differences between Scotland and the rest of Great Britain;

(b) the additional transport costs involved in supplying Scottish customers from dairies in northern England;

(c) the market shares of the major processors established in northern England and in Scotland, and the extent of trade between the two locations;

(d) the means of local distribution to supply middle-ground customers in Scotland;

(e) the preferences of Scottish consumers; and

(f) the corporate strategies of the major processors, in northern England and in Scotland.

1.8. The Commission Group charged with conducting this inquiry (the Group) was divided about what conclusions to draw from this analysis. Two members, Mr Clothier and Mr Mackay, concluded that conditions in Scotland had continued to move closer to those in the rest of Great Britain since the Commission last looked at this issue in 1996 and that the point had now been reached where there was a single Great Britain market for the supply of fresh processed milk to both the larger and smaller supermarkets and to other large middle-ground retail chains and symbol groups—although supply to the diminishing number of smaller independent stores (which Wiseman estimated accounted for some 20 per cent, by volume, of the milk sold through shops) continued to constitute a separate Scottish market. The other two members, Mrs Kingsmill and Professor Cave, concluded that the supply of fresh processed milk to all categories of middle-ground retailers in Scotland constituted a separate market.

1.9. All members of the Group concluded that the division of retailers into the three groups included in our terms of reference (larger supermarkets, middle-ground retailers and doorstep deliveries) was valid—although they considered that the purchasing patterns of many larger middle-ground retailers were becoming more like those of the larger supermarkets.

1.10. The Group also agreed that, from an economic perspective, 'middle-ground customers' might be a more appropriate way of categorizing this market segment, than the 'middle-ground retailers' included in our terms of reference. The wider category would also include non-retailers such as the NHS, local authorities, the Ministry of Defence, schools, caterers, etc.

1.11. The Group then turned to providing specific answers to the five questions posed by the DGFT.

1.12. It concluded that, in the terms of the Act, there was a monopoly in the supply of fresh processed milk to middle-ground retailers in Scotland, which existed in favour of Wiseman.

1.13. It then examined Wisemans's behaviour, both currently and over the last few years, to see if it had taken any steps to exploit or maintain that monopoly, or whether any of its actions or omissions was attributable to it.

1.14. Mrs Kingsmill and Professor Cave concluded that Wiseman's conduct between 1996 and 1998 in respect of charging excess prices (ie above competitive levels) was a step taken for the purpose of maintaining its monopoly position; and that its failure to compete with Claymore Dairies in the period before December 1998 constituted an omission attributable to the monopoly. Mr Clothier and Mr Mackey dissented from both conclusions.

1.15. All members of the Group concluded that Wiseman's acquisition of Gilmour's Dairy Limited and of the Aberdeen Milk Company Limited and the subsequent closing down of their processing capacity were steps that were likely to have been taken, at least in part, for the purpose of maintaining its monopoly position, and that its actions were likely to have been, to some extent, attributable to it.

1.16. Mrs Kingsmill and Professor Cave concluded that the fact that Wiseman sought an exclusive supply agreement with Aberness Foods Ltd, and paid over £[✂] in connection with it, was a step taken for the purpose of maintaining its monopoly position. Mr Clothier and Mr Mackay dissented from this conclusion.

1.17. Next, Mrs Kingsmill and Professor Cave concluded that Wiseman's entering into contracts with former customers of Express/Claymore at prices which did not cover their total average costs—and, on certain assumptions, average variable costs—was for the purpose of undermining Express/Claymore's continued presence in Scotland and constituted uncompetitive steps taken by Wiseman for the purpose of exploiting and maintaining its monopoly position. Mr Clothier and Mr Mackay, in part because they did not agree that these all-Scotland contracts should be viewed on an incremental basis, dissented from these conclusions, but themselves concluded that the speed and wide-ranging manner in which Wiseman went about targeting Express/Claymore's major customers in northern Scotland in the period immediately after Express acquired its controlling stake was a step that could have had as part of its purpose the maintenance of its monopoly position—although they do not regard it as being by way of an uncompetitive practice.

1.18. The Group concluded its investigation by considering whether any of the facts that it had found operated, or might be expected to operate, against the public interest. Mrs Kingsmill and Professor Cave concluded that they did; Mr Clothier and Mr Mackay concluded that they did not.

1.19. The Chairman of the Group, Mrs Kingsmill, used her casting vote in favour of the conclusion that these facts did operate, or might be expected to operate, against the public interest. But as less than two-thirds of the members of the Group supported this conclusion it does not form a basis upon which the Secretary of State would be in a position to impose remedies. Consequently, the Group did not consider any.