Anticipated acquisition by Heineken N.V. of Diageo plc assets

ME/6576/15

The CMA's decision on reference under section 33(1) of the Enterprise Act 2002 given on 18 December 2015. Full text of the decision published on 27 January 2016.

Please note that [✂] indicates figures or text which have been deleted or replaced in ranges at the request of the parties for reasons of commercial confidentiality.

SUMMARY

1. On 7 October 2015, Heineken N.V. (**Heineken**) acquired sole control over a number of subsidiaries of Diageo plc (**Diageo**), including of Desnoes & Geddes Limited (**D&G**).

2. The overall and staggered acquisition by Heineken of some assets and shares owned (directly or indirectly) by Diageo (the **Diageo business**), including the transfer of licensing arrangements of the Red Stripe, Dragon Stout and D&G Malta brands (the **Target Brands**) is hereafter referred as the **Merger**. Heineken and the Diageo business are together referred to as the **Parties**.

3. The Competition and Markets Authority (**CMA**) considers that the Parties will cease to be distinct and that the share of supply test is met. The CMA therefore considers that arrangements are in progress or in contemplation which, if carried into effect will result in the creation of a relevant merger situation.

4. The CMA has considered the impact of the Merger on the basis of the narrowest plausible frames of reference, which are:

(a) the supply of premium lager[1] to the on-trade channel[2] in Great Britain (**GB**); and

(b) the supply of premium lager to the off-trade[3] channel in GB.

5. The Merger will lead to only a small increment in the share of supply in both frames of reference. In addition, the merged entity will remain constrained by several other premium lager brands that compete more closely with Heineken than Red Stripe. The CMA therefore concluded that the Merger will not give rise to a realistic prospect of a substantial lessening of competition (**SLC**).

6. The Merger will therefore **not be referred** under section 33(1) of the Enterprise Act 2002[4] (the **Act**).

ASSESSMENT

Parties

7. Heineken N.V. is the holding company of the Heineken Group, an international group active in the production, commercialisation and distribution of beer and other beverages world-wide. In the United Kingdom (**UK**), Heineken has a broad portfolio of brands (eg owning 22 beer brands, including 9 premium lagers). The main brands of beers it supplies in the UK Heineken, Foster's, Kronenbourg 1664, John Smith's, Tiger, Amstel, Sol, Desperados, Deuchars and Newcastle Brown Ale. In the financial year ended 31 December 2014, the Heineken Group had worldwide revenues of approximately £15.53 billion of which £1.22 billion derived from sales in the UK.

8. Diageo is a global consumer company active in the production, distribution, marketing, exporting and importing of beer and spirits world-wide. Diageo, through its subsidiary D&G (a company listed on the Jamaican Stock Exchange) owned the following brands distributed in GB: Red Stripe (a lager), Dragon Stout (a stout) and D&G Malta (a non-alcoholic malt-based drink). In the financial year ended 30 June 2015, Diageo's revenue derived from the sales of the Target Brands in the UK was [✂].

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[1] For the purpose of this decision, 'premium lager' means a lager with an alcohol content above 4.3% alcohol by volume (**ABV**), whilst a 'standard lager' has an alcohol content below 4.3% ABV. This definition is supported by third party submissions and previous decisions of the CMA predecessors (see paragraph 24).
[2] Ie sold in pubs, bars and restaurants.
[3] Ie sold in retail outlets.
[4] As modified by Article 3 of the Enterprise Act 2002 (Anticipated Mergers) Order, SI No. 2003/1595).

Transaction

9. On 7 October 2015, Heineken completed the acquisition of the following Diageo subsidiaries:

   (a) D&G – who owns the Target Brands – by increasing its shareholding in this company from 15% to 73%.

   (b) GAPL Pte Ltd – a Singapore-based company – by increasing its shareholding in this company from 50.1% to 100%.

10. The Target Brands are currently licensed in GB to Diageo Great Britain Limited (Diageo GB), who also has the distribution rights for these brands. Pursuant to the Framework Agreement[5] dated 7 October 2015, Heineken will acquire these licensing and distribution rights on 1 January 2016.

11. The CMA considers that Heineken has already, on 7 October 2015, acquired legal control[6] over D&G who owned the Target Brands and material influence over the Target Brands in GB.[7] This acquisition of material influence is further supported by the *Manufacturing, Bottling, Selling, Distribution, and Marketing Agreement* that is currently in place between D&G (now controlled by Heineken) and Diageo GB. This agreement [✂]. However, with the transfer of the licence and distribution rights of the Target Brands to Heineken, Heineken will acquire a higher level of control ('legal' control) over these brands.

12. The CMA considers that the two stages by which Heineken is acquiring control over the Target Brands in GB may be treated together under section 29(2)-(4)[8] of the Act, since they occur within two years and confer different levels of control over the same enterprise. Pursuant to section 29(1)[9] of the Act, the CMA believes, applying its discretion, that it is appropriate to treat the successive events described above as occurring on the date the latest of them takes place, namely 1 January 2016. Therefore, the Merger will be treated as an anticipated Merger.[10]

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[5] Framework agreement entered into between Grand Metropolitan and Heineken International BV on 7 October 2015.
[6] *Mergers: Guidance on the CMA's jurisdiction and procedure* (CMA2), January 2014, paragraphs 4.12 & 4.30.
[7] *Mergers: Guidance on the CMA's jurisdiction and procedure*, paragraphs 4.14–4.17.
[8] As amended by the Enterprise Act 2002 (Anticipated Mergers) Order, SI No. 2003/1595.
[9] As amended by the Enterprise Act 2002 (Anticipated Mergers) Order, SI No. 2003/1595.
[10] The Parties informed the CMA that the Merger is also the subject of review by the Competition Commission in Singapore.

Jurisdiction

13. As a result of the Merger, the enterprises of Heineken and the Diageo business will cease to be distinct.

14. The Parties' main overlap is in the supply of premium lager to the on-trade and off-trade channels in GB. The Parties' combined share of supply of premium lager to the on-trade channel in GB is [30–40%], with an increment of around [0–5%] (see Table 1 below). The CMA therefore considers that the share of supply test in section 23 of the Act is met.

15. The CMA therefore believes that it is or may be the case that arrangements are in progress or in contemplation which, if carried into effect, will result in the creation of a relevant merger situation.

16. The initial period for consideration of the Merger under section 34ZA(3) of the Act started on 20 November 2015 and the statutory 40 working day deadline for a decision is therefore 19 January 2016.

Counterfactual

17. The CMA assesses a merger's impact relative to the situation that would prevail absent the merger (ie the counterfactual). For anticipated mergers the CMA generally adopts the prevailing conditions of competition as the counterfactual against which to assess the impact of the merger. However, the CMA will assess the merger against an alternative counterfactual where, based on the evidence available to it, it considers that, in the absence of the merger, the prospect of these conditions continuing is not realistic, or there is a realistic prospect of a counterfactual that is more competitive as between the parties than these conditions.[11]

18. In this case, there is no evidence supporting an alternative counterfactual, and neither the Parties nor any third parties have put forward arguments in this respect. Therefore, the CMA considers the prevailing conditions[12] to be the relevant counterfactual.

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[11] *Merger Assessment Guidelines* (OFT1254/CC2), September 2010, from paragraph 4.3.5. The *Merger Assessment Guidelines* have been adopted by the CMA (see *Mergers: Guidance on the CMA's jurisdiction and procedure* (CMA2), January 2014, Annex D).

[12] For the purpose of this case, prevailing conditions means, interpreted pursuant section 29(1) of the Act, the conditions of competition prior to the acquisition by Heineken of any level of control over the Diageo assets (7 October 2015).

Frame of reference

19. The CMA considers that market definition provides a framework for assessing the competitive effects of a merger and involves an element of judgement. The boundaries of the market do not determine the outcome of the analysis of the competitive effects of the merger, as it is recognised that there can be constraints on merger parties from outside the relevant market, segmentation within the relevant market, or other ways in which some constraints are more important than others. The CMA will take these factors into account in its competitive assessment.[13]

Overlap between the parties

20. Heineken supplies both premium lagers (ie Kronenbourg 1664, Heineken, Desperados) and non-premium lagers (eg Amstel, Foster), as well as stout (Murphy's Irish Stout) in the UK. Heineken is not active in the supply of any non-alcoholic malt-based drink in the UK.

21. The Diageo business includes the Target Brands that are distributed in GB.[14] The Target Brands are not directly sold in Northern Ireland by Diageo GB, although Diageo submitted that there may be some indirect sales of the Target Brands in Northern Ireland by wholesalers.[15]

22. Therefore, the Parties overlap in the supply of premium lager and stout in GB.

23. With regard to the supply of stout, the annual sales of Dragon Stout in GB do not exceed [✂] and Heineken's own sales of stout in the UK are around [✂] resulting in a combined share of supply of stout in GB of less than [0–5%]. As such, the CMA therefore considers that the Merger will not give rise to an SLC in the supply of stout in GB.

Product scope

24. In previous decisions, the CMA's predecessors[16] and the European Commission,[17] considered that the supply of beer could be segmented by

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[13] *Merger Assessment Guidelines*, paragraph 5.2.2.
[14] Diageo currently brews most of the Red Stripe sold in Great Britain at its St. James's Gate brewery in Dublin. [✂]
[15] Northern Ireland will therefore not be considered further in this decision.
[16] For instance, the OFT's decision on the *Anticipated acquisition by InBev NV/SA of Anheuser-Busch Companies, Inc* (ME/3826/08), of 18 November 2008; and the Competition Commission's decision on the *Anticipated acquisition by Interbrew SA of the brewing interests of Bass plc*, of January 2001.
[17] For instance, the decisions of the European Commission on the following cases: *COMP/M.4999 Heineken / Scottish & Newcastle Assets,* 3 April 2008; *COMP/M.4952 - Carlsberg / Scottish & Newcastle Assets,* 3 March 2008; *COMP/M.3032 - Interbrew / Brauergilde*, 19 December 2002; and *COMP/M.2569 - Interbrew / Beck's,* 26 October 2001.

type of beer (eg lager, ale, stout), alcohol content (premium and standard (as defined in footnote 1) and sale channel (off-trade and on-trade channels, as defined in footnotes 2 and 3).

25. Heineken acknowledged these precedents in their submission and have not proposed or presented any reasons for the CMA to depart from them.

26. The majority of third parties that responded to the CMA's investigation distinguished between premium lager and standard lager based on the level of alcohol content. A minority of third party respondents, however, submitted that premium and standard lager can be distinguished not only in terms of alcohol content, but also in terms of price, provenance, quality, authenticity, style and image.

27. Based on the evidence available to it, in particular third party responses to its merger investigation, the CMA considers that there is little demand-side substitution between the on and off-trade channels and that the portfolio of beers available in each channel differs to some extent. On the supply side, the CMA considers that these two channels vary significantly, based on third party submissions on the requirements for entry or expansion in each of these channels (eg upfront investment required to launch a new brand in the off-trade channel and fragmented nature of the on-trade channel which requires a wider distribution system).

28. In summary, the CMA assessed the Merger by reference to the supply of premium lager to each of the on-trade and off-trade channels. However, the CMA considers it was not necessary to determine conclusively the relevant product frames of reference, since, as set out below, no competition concerns arise even on the narrowest plausible basis.

Geographic scope

29. As mentioned above, the Parties overlap in the supply of lager in the UK.

30. The European Commission has historically considered the market for the production and distribution of beer to be national in scope.[18] Previous decisions of the CMA's predecessors found that the appropriate geographic frame of reference for the assessment of a merger involving the supply of beer was the UK or, at its narrowest, GB and Northern Ireland separately.[19]

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[18] See, for instance, the decisions mentioned in footnote 17.
[19] See, for instance, the OFT's decision on the *Anticipated acquisition by InBev NV/SA of Anheuser-Busch Companies, Inc* (ME/3826/08), of 18 November 2008.

31. Heineken acknowledged these precedents in their submission and have not proposed or presented any reasons for the CMA to depart from them.

32. The majority of third parties that responded to the CMA's merger investigation submitted that the supply of lager is national or GB wide. Some third parties noted, on the one hand, the increased presence of imported beers and, on the other hand, the very small degree of regional variation with the presence of some lager being limited or stronger in some regions (eg Tennent's Lager in Scotland).

33. In summary, the CMA therefore assessed the Merger on the basis of a GB wide geographic scope. It was not necessary for the CMA to reach a conclusion on the precise geographic frame of reference in this case, since, as set out below, no competition concerns arise even on the narrowest plausible basis.

Conclusion on frame of reference

34. For the reasons set out above, the CMA has considered the impact of the Merger on the basis of the following frames of reference:

   (a) The supply of premium lager to the on-trade channel in GB.

   (b) The supply of premium lager to the off-trade channel in GB.

Competitive assessment

Horizontal unilateral effects

35. Horizontal unilateral effects may arise when one firm merges with a competitor that previously provided a competitive constraint, allowing the merged firm profitably to raise prices or degrade quality on its own and without needing to coordinate with its rivals.[20] Horizontal unilateral effects are more likely when the merger parties are close competitors. The CMA assessed whether it is or may be the case that the Merger may be expected to result, in an SLC in relation to unilateral horizontal effects in:

   (a) the supply of premium lager to the on-trade channel in GB; and

   (b) the supply of premium lager to the off-trade channel in GB.

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[20] *Merger Assessment Guidelines*, from paragraph 5.4.1.

Shares of supply

36. Table 1 below shows the shares of the Parties and their leading competitors, by volume, in 2014,[21] in the supply of: (i) premium lager to the on-trade channel in GB; and (ii) premium lager to the off-trade channel in GB.

Table 1: Shares in the supply in the on-trade and off-trade premium lager segments in Great Britain

	Share by volume (%)	
Supplier	*On-trade premium lager*	*Off-trade premium lager*
Heineken	[20–30]	[10–20]
Red Stripe	[0–5]	[0–5]
Combined share	[30–40]	[10–20]
AB InBev	[20–30]	[50–60]
Miller	[20–30]	
Carlsberg	[10–20]	[10–20]
Molson Coors	[5–10]	[0–5]
Others	[5–10]	[5–10]
Total	100	100

Source: Heineken's estimates based on *CGA Strategy – Global trade consulting*; and Diageo's internal sales figures.

37. Heineken's share of supply of premium lager in GB is less than 30% in both the on-trade and off-trade channels ([20–30%] and [20–30%] respectively). The Merger results in a very small increment to Heineken's share of supply: [5–10%] and [0–5%] respectively.

38. There are three other competitors with a significant presence in both the on-trade and off-trade premium lager segment (AB InBev and Carlsberg) as well as a tail of other competitors. Furthermore, Miller has a strong presence in the on-trade premium lager segment.

39. The evidence submitted by Heineken also supports that the merged entity will remain constrained by other premium lager suppliers and that the Merger will not substantially change Heineken's market position:

(a) The Canadean Beer Market Insights report (2014) lists the top ten premium beer brands in the UK by volume. Two of Heineken's brands are listed in the top ten (Kronenbourg 1664 and Heineken). The other brands listed are owned by AB InBev, SAB Miller, Molson Coors, Carlsberg and Diageo. Red Stripe is not listed.

(b) Diageo's presence in the on-trade market is very limited. [✂]

[21] All the figures are for 2014 (calendar year), except the Red Stripe figures that refer to the 12 months ending 30 June 2015.

Closeness of competition

40. Heineken submits that Red Stripe is not an especially close competitor to the premium lager brands that Heineken already distributes in GB. Heineken considers that its brands that could be viewed as relatively close competitors to Red Stripe are Heineken, Kronenbourg 1664 and Sol. The Parties' internal documents support these submissions. Whilst Diageo's internal documents show that the marketing of Red Stripe is targeted at [✄], Heineken's internal documents indicate that [✄]

41. Some third parties who replied to the CMA's investigation identified Heineken's brands as competing with Red Stripe (Kronenbourg 1664, Heineken, Birra Moretti, Amstell, Tiger). The majority of the third parties described Red Stripe as a 'niche', 'unique' or 'world beer' brand with different target customers from the lagers in Heineken's portfolio. Some customers also noted that Red Stripe has a very small presence in the on-trade channel and one customer stated that, in this channel, Red Stripe is only available in some London outlets.

42. All third parties also identified brands owned or distributed by other competitors as competing with Red Stripe, eg San Miguel, Corona (Carlsberg), Stella Artois, Brahma (AB InBev), Grolsch (Molson Coors). Some third party customers also stated that 'there are a wealth of brands on the market' including lagers imported from other countries or that 'there is a very large and varied market in the UK'.

Conclusion on horizontal unilateral effects

43. As set out above, the CMA considers that the Merger will lead to only a small increment of Heineken's share in both the on-trade and off-trade premium lager segments in GB. After the Merger, Heineken remains constrained by other premium lager brands that compete more closely with Heineken than Red Stripe. The CMA therefore believes that the Merger will not give rise to a realistic prospect of an SLC as a result of horizontal unilateral effects in the supply of premium lager to each of the on-trade and off-trade channels in GB.

Conglomerate effects

44. Conglomerate effects may arise in mergers of firms that are active in the supply of goods or services that do not form part of the same markets but which are nevertheless related in some way, either because their products are complements (so that a fall in the price of one good increases the customer's

demand for another) or because there are economies of scale in purchasing them (so that customers buy them together).[22]

45. The CMA's approach to assessing conglomerate theories of harm is to analyse whether the merged entity would have: *(a)* the ability to foreclose competitors; *(b)* its incentive to do so; and *(c)* whether any action by the merged firm would be sufficient to reduce competition in the affected market.[23] To reach an SLC finding, all three questions must be answered in the affirmative.

46. Two competitors who replied to the CMA's merger investigation expressed concerns regarding the potential conglomerate effects of the Merger. One competitor in particular stated that by adding Red Stripe to its portfolio, Heineken will be able to leverage its strength to have retailers list Red Stripe at the expense of smaller competitors.

47. However, the evidence available to the CMA does not indicate that the Merger will enhance Heineken's ability to foreclose its competitors as a result of the integration of the Target Brands in its portfolio, in particular because:

   (a) replies from third parties indicate that Red Stripe has a very small presence in GB and is not a 'must have' brand;

   (b) although Heineken has a broad portfolio of brands (see paragraph 7 above) other competitors have an equally extensive portfolio;[24] and

   (c) the evidence available to the CMA does not indicate that Heineken is conditioning sales of some or all of its brands on the purchase of any of its other brands. All of Heineken's customers that responded to the CMA's merger investigation said they multisource beer from different suppliers.

48. The CMA therefore considers that the Merger will not result in the merged entity having the ability to engage in a foreclosure strategy, for instance by insisting that its customers buy its full range of products.[25]

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[22] Most non-horizontal mergers are considered to be benign or even efficiency-enhancing (when they involve complementary products) and do not raise competition concerns. However, in certain circumstances, a conglomerate merger can result in the merged entity foreclosing rivals, including through a tying or bundling strategy. *Merger Assessment Guidelines*, paragraph 5.6.2.
[23] *Merger Assessment Guidelines*, paragraph 5.6.6.
[24] For example: (i) AB InBev has a portfolio of 15 'beer' brands, including 13 premium lager; (ii) Molson Coors has a portfolio of 16 'beers', including 6 premium lagers; (iii) Carlsberg has a portfolio of 13 'beers' including 8 lagers. These competitors seem to match Heineken's portfolio of brands even with the addition of Red Stripe and the other Target Brands.
[25] As such, the CMA does not proceed to assess if the merged firm would have incentives to do so and concludes that there is no realistic prospect of an SLC arising as a result of conglomerate effects.

Conclusion on conglomerate effects

49. The CMA therefore believes that the Merger will not give rise to a realistic prospect of an SLC as a result of conglomerate effects in relation to the supply of premium lager to each the on-trade and off-trade channels in GB.

Third party views

50. The CMA contacted customers and competitors of the Parties as well as industry associations.

51. Third party comments have been taken into account where appropriate in the competitive assessment above.

Conclusion on substantial lessening of competition

52. Based on the evidence set out above, the CMA does not believe that the Merger will give rise to a realistic prospect of an SLC in: (i) the supply of premium lager to the on-trade and/or off-trade channels in GB; or (ii) in the supply of stout in GB to the on-trade and/or off-trade channels.

53. Consequently, the CMA does not believe that it is or may be the case that the Merger may be expected to result in an SLC within a market or markets in the United Kingdom.

54. The Merger will therefore not be referred under section 33(1) of the Act.

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Competition and Markets Authority
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