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## **Anticipated merger between J Sainsbury Plc and Asda Group Ltd Issues Statement**

Which? welcomes the opportunity to provide comments to the Issues Statement, in relation to the in-depth investigation into the proposed merger between J Sainsbury Plc and Asda Group Ltd.

The grocery sector is one of the most widely-used and important consumer markets in the UK. Over the past decade, the UK grocery sector has seen innovation through competition that has delivered a good deal for consumers on a number of levels. Price has been an important factor, but competition has also led to a much wider and very important range of consumer benefits in the form of better quality and range of products.

Some UK retailers through private standards have, for example, pre-empted or gone beyond regulation in their desire to assure consumers that they can meet their needs for food safety, but also wider quality. Growing competition from discount chains Aldi and Lidl highlight the positive impact that competition can have on outcomes for consumers. The discounters have steadily increased their market share in recent years and put pressure on other supermarkets to innovate. This has partly been about offering lower prices, but has also encouraged innovation in the range, quality and choice that is on offer to consumers – as well as how and where products have been produced.

Therefore, it is important that the CMA fully considers all the impacts that this merger could have on the incentives for companies in the UK grocery sector to offer value for money products, improve quality and introduce new and better products in both the short and long-term.

### **This merger requires a high standard of proof and evidence on all possible consumer outcomes**

There is often considerable uncertainty in assessing mergers, as to both the likely competitive effects of the merger and the specific manner in which those effects will manifest in the market in the post-merger world. In particular, it is relatively difficult to consider the potential impacts on non-price outcomes such as quality and choice. Given those challenges, the importance of this market for consumers and the fact that this market is already very concentrated, the standard of proof and threshold that this merger needs to meet to get through must be sufficiently high to ensure the merger will not harm consumers in the short or long-term. The CMA must make sure it gathers sufficient, accurate and reliable qualitative and quantitative evidence on possible impacts on *all* consumer outcomes.

### **The assessment of the competitive effects of the merger must consider impacts on price, quality, range of services and innovation**

We agree with the CMA that in considering the horizontal unilateral effects of this merger it needs to consider whether the merged company could not only increase prices, but also



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lower quality, reduce the range of products and services and reduce innovation in the market following the merger.

Our consumer research on food shows that the price of food is important for consumers but alongside high expectations of safety and quality. When we asked consumers whether they would buy food items produced to lower quality standards (i.e. how the food has been produced and its ingredients) if they were cheaper than at present, 71% said that they would not buy.<sup>1</sup> There was no observable difference in opinion when looking at the household social grade of the respondent. 71% of those from higher social grade households (AB) said they wouldn't buy cheaper, lower quality food, compared to 68% of those from lower social grade households (DE).

When we asked consumers if they would switch the stores where they do their majority shopping if (a) food prices were to increase by 5-10%, 39% said that it was likely that they would switch and (b) if standards went down, 49% said that it was likely that they would switch. This shows that for consumers both prices and standards are important. In fact they are more likely to say they would switch supermarket if standards were lowered than if prices increased.

Our survey also found that Asda customers were significantly more likely (46%) than Sainsbury's customers (35%) to say that they would be likely to switch if prices were to increase by 5-10%.<sup>2</sup>

### **The assessment of the competitive effects must also consider the impact of a potential increase in buyer power on consumer outcomes**

We agree with the CMA that in investigating the possible impact of this merger, it needs to consider whether the merged company would have increased buyer power to the extent that the merger might distort competition in the groceries market and result in adverse effects for consumers.

The CMA is proposing two theories of harm in relation to this:

- Theory of harm A: if the merged company has significant market power it could force the price down towards the marginal cost of supplying the products and that this could reduce the incentive for suppliers to invest.
- Theory of harm B: the merged company may raise the purchasing costs of rival retailers, which under certain circumstances, may result in price increases to certain customers (the "waterbed effect").

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<sup>1</sup> Populus, on behalf of Which?, surveyed 2107 UK adults online between 17th-18th January 2018. The data were weighted to be demographically representative of the UK population. <https://consumerinsight.which.co.uk/articles/brexitandfood>.

<sup>2</sup> Populus, on behalf of Which?, surveyed 2399 online between 17-18th October 2018. The data were weighted to be demographically representative of the population. The base sizes for these results are 333 and 267 respectively.



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In relation of theory of harm A, there may be a second effect if the merged firm chooses to consolidate its suppliers. Since a supplier's expected profits from investing in new products depend on the total volume that they expect to sell to supermarkets then a supplier needs to consider the probability that the new product would be stocked by each supermarket. If the merged firm has fewer suppliers overall then this probability may fall. This would reduce the supplier's expected profits and their incentive to innovate, ultimately leading to less consumer choice.

Diversity and choice in terms of sourcing and supply is important. We know from our consumer research, for example, that many people also want to support UK producers. Our Brexit consumer tracker survey (January 2018) found that three quarters or more of consumers thought that it was important that milk, eggs, other dairy products and poultry were produced in the UK.

Food supply chains are often complex, global and integrated. In assessing any impact this merger will have on competition, it is important that the CMA looks closely at the implications across different supply chains and what this might mean for standards, choice and sourcing, as well as price effects.

Finally, this proposed merger is coming at an important time for the UK food and grocery supply chain as the UK leaves the EU. The nature of Brexit and decisions about what type of food and farming policy the UK has going forward present both opportunities and risks – including for food security, resilience, choice and standards. It is important that the CMA considers the impact of a merger on this scale for consumers now and in the years ahead against this backdrop of uncertainty, and potentially some fundamental market and supply chain changes.

### **The assessment of the competitive effects should consider the impact on consumer search of maintaining both Asda and Sainsbury's brands**

The parties are proposing to retain the separate branding of the two firms post-merger. It is argued that this is to the benefit of consumers since it allows a differentiated retail offering catering to the differing consumer preferences of their customers. However, Asda and Sainsbury's are also direct competitors. When asked which supermarket brand a consumer would they be most likely to switch to if standards went down 25% of Asda customers told us that they would switch to Sainsbury's and 17% of Sainsbury's customers told us that they would switch to Asda,<sup>3</sup> while in a switch prompted by a price rise, 19% of Sainsbury's customers say they would switch to Asda and 12% of Asda customers would switch to Sainsbury's.<sup>4</sup>

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<sup>3</sup> Populus, on behalf of Which?, surveyed 2399 online between 17-18th October 2018. The data were weighted to be demographically representative of the population. 157 Asda customers and 144 of Sainsbury's customers answered this question.

<sup>4</sup> Populus, on behalf of Which?, surveyed 2399 online between 17-18th October 2018. The data were weighted to be demographically representative of the population. 96 of Sainsbury's customers and 152 of Asda customers answered this question.



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The CMA should therefore consider the impact on consumer search, and hence on competition, of having one firm operating two brands that are perceived as being competitors. Norman Ireland (Journal of Industrial Economics, 2007)<sup>5</sup> shows that in the case where a retailer owns two brands it can obfuscate consumer search as some consumers needlessly search both brands. It obtains monopoly power over those consumers who only search two shops and happen to sample just those two. This means those consumers are at risk of a bad purchase, but also the lack of transparency and the reduction in effective consumer search in the market could also reduce the overall level of competition.

### **Any consideration of any merger specific efficiencies must focus on consumer outcomes**

The parties have announced that the merger would deliver £500 million in cost efficiencies and that this will allow them to reduce prices for consumers. It isn't clear what proportion of those efficiencies the companies are suggesting would be passed on to consumers as opposed to their shareholders.

We fully agree with the CMA that consideration of any merger specific efficiencies must focus on the "likelihood of these savings being passed onto consumers" in the short and long-term. The CMA needs to make sure it has accurate and impartial evidence to look at this. We would argue that given the importance of this sector for consumers, unless the CMA has sufficient certainty that those efficiencies would deliver positive outcomes for consumers, they should not be taken into consideration as a countervailing factor likely to prevent or mitigate substantial lessening of competition (SLC).

### **About Which?**

Which? is the largest consumer organisation in the UK with more than 1.3 million members and supporters. We operate as an independent, a-political, social enterprise working for all consumers. We are funded solely by our commercial ventures and receive no government money, public donations, or other fundraising income. Which?'s mission is to make individuals as powerful as the organisations they have to deal with in their daily lives, by empowering them to make informed decisions and by campaigning to make people's lives fairer, simpler and safer.

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<sup>5</sup> Ireland, N. J., 2007, "Posting Multiple Prices to Reduce the Effectiveness of Consumer Price Search", *The Journal of Industrial Economics*, No2, pp. 235-263.