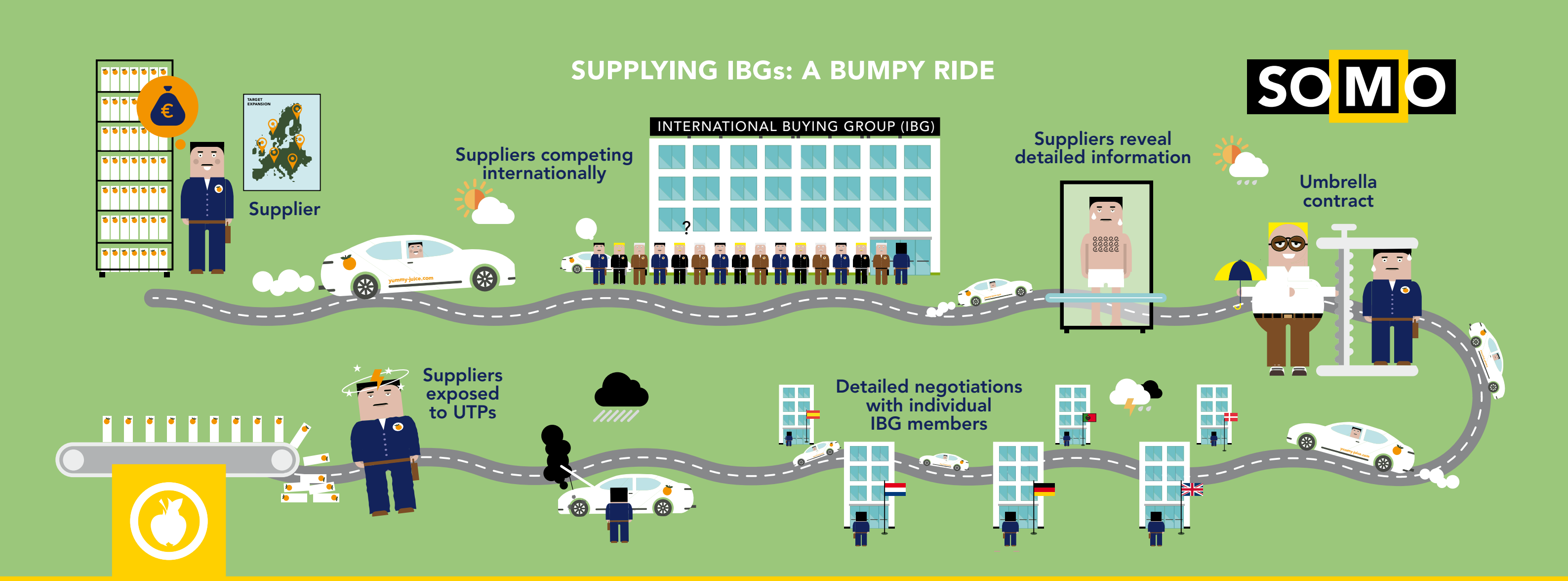


Eyes on the price

International supermarket buying groups in Europe

SOMO Paper | March 2017

European retailers are in fierce competition with each other over market share. They are continuously expanding the number of stores, attempting to reduce operational costs, developing private label products (a retailer's own brand), or taking over competitors nationally and internationally. In this process, supermarkets have gained extensive buying power,* which gives them leverage to extract ever lower prices from their suppliers. One strategy through which supermarkets aim to increase their buyer power is to cooperate in cross-border buying groups.

Supermarkets in Europe have a powerful position in the food supply chain because they are often the single most important food retail outlet. In 11 different European countries, fewer than eight retail chains control the vast majority of the nation's food retail.[1] For example, five retailers make up 85 per cent[2] of the German market in 2014 and 77 per cent[3] of the Dutch market in 2016. Retail is also continuously concentrating in most European countries.[4] Retailers have a powerful influence over which food products are sold and at what price, since producers and suppliers are highly dependent on supermarkets to sell their products. The number of corporations in the food supply chain varies from country to country; yet the hourglass shaped form of the Dutch retail market roughly applies to countries across Europe (see Figure 1). The model illustrates that there are just a few retailers through which food finds its way from a large number of farmers to a smaller number of suppliers and on to millions of consumers. In the case of the Netherlands, many smaller supermarkets work together in a national buying group with the result that just five companies effectively control practically all food retailing in this country.[5]

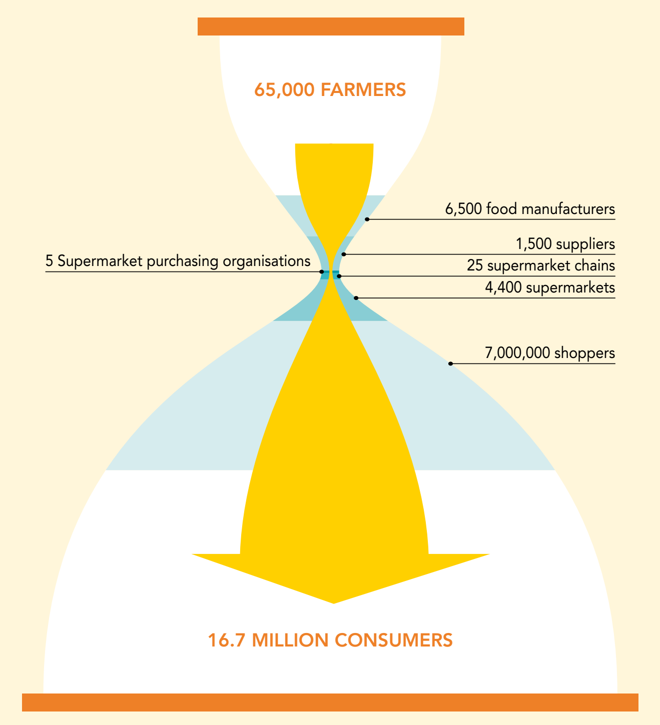
Unfair trading practices

The increasing scale of operations of large retailers allows them to negotiate ever more favourable terms and conditions with suppliers.** Over the past ten years, the growing imbalance of bargaining power within food supply chains in relation to concerns over negative economic and social impacts on producers and processors has led to intensified debate at the European Union (EU) level. In particular the issue of unfair trading practices (UTPs) in food supply chains has attracted a lot of attention from EU regulators.[6]

* The term 'buying power' refers to the ability to influence the terms of trade with upstream suppliers and the leverage of retail companies over suppliers. This report does not use the normative classification used by economists and competition lawyers.

** There are a number of very large manufacturers operating in this sector that probably have a reasonable bargaining position in negotiations with supermarkets because of their size and customer brand loyalty.

Figure 1 **Concentration of power in the Dutch food supply chain**



Source: PBL: Netherlands Environmental Assessment Agency

UTPs can be defined as practices that grossly deviate from good commercial conduct, good faith and fair dealing, and that are unilaterally imposed by one trading partner onto another.[7] Research and investigative media reports[8] show that they are also applied by retailers (also see Box 1 and Box 5). Research has also exposed how UTPs impact on consumer prices and product variety, suppliers' profitability and competitiveness, and working conditions in the developing world.[9] For example, retailers' price pressure results in poor working conditions in the banana and pineapple production in Costa Rica and Ecuador[10], and the Indian cashew processing industry.[11]

International cooperation

In order to achieve economies of scale and reduce operational costs, supermarket chains cooperate at both national and international level. International level cooperation takes form in so-called international buying groups (IBGs) or international buying alliances. These are groups of supermarket chains that coordinate procurement across borders to obtain the lowest possible prices for well-known brands and/or basic private label groceries. Even though there is ample evidence of the buying power of European supermarket chains[12] and national buying alliances have occasionally been subject to investigations by competition authorities,[13] the role of IBGs in increasing supermarket buying power has not been the subject of systematic research yet.

Aim, methodology and respondent participation

This briefing paper sheds some light on how IBGs work, how they contribute to supermarket buying power and how they might affect market conditions – including the relationship between supermarkets and their suppliers. It will look more closely at how two prominent IBGs work: European Marketing Distribution (EMD) and Associated Marketing Services (AMS). The findings are intended to support civil society organisations that are working towards improving environmental and social standards in food and agricultural supply chains. Ultimately, this report aims to influence and improve both the policies and the practices of retailers, as well as EU policy to ensure fair and sustainable food supply chains globally.

Box 1 **Gaining more buying power**

The merger of European retailers Ahold and Delhaize in July 2016 is illustrative for the retail sector. The merger created a new European top-five food retail company. The new retailer looked for new ways to cut costs in its sourcing and invited about 100 of their largest suppliers in the Benelux for meetings to align differences in purchasing prices and conditions with their sourcing department, before the official annual negotiations started. According to food business media, suppliers were informed that they would have to offer retroactive price discounts. After Kraft Heinz refused to have this meeting, Ahold Delhaize temporarily took Heinz products off their shelves (known as 'delisting').[14] The Federation of Dutch Food and Grocery Industry (FNLI) wanted to register a complaint against Ahold Delhaize for demanding concessions from suppliers; according to them, this was in violation of the industry code for fair business practices, which Ahold Delhaize has signed.[15] However the steering committee of the code of conduct could not take the complaint into account, apparently its complaints handling facility was not able to handle the claims and/or it was dismantled shortly before.[16]

The analysis is based on literature research and interviews with experts in the sector. Emails requesting cooperation in the research were sent to manufacturers (17), retailers involved in IBGs (3), independent experts from the grocery sector (10) and buying groups (EMD and AMS). Most of the parties did not respond to the request at all. Others stated they were not in the position to be interviewed. AMS, for example, stated that their answers might contain confidential information. Two buying group experts did not feel comfortable cooperating with the research because of confidentiality clauses or loyalty concerns to current CEOs of buying groups or retailers.

Eight people were willing to take part in the interviews, including two Dutch specialists on private labels, Superunie (a Dutch national level buying alliance and member of EMD), the managing director of EMD and three biscuit and juice manufacturers. Albert Heijn, the Dutch supermarket operating under the banner of the Ahold Delhaize group (and a member of buying group AMS), stated that it could not respond to questions about specific products, specific suppliers, volumes and the legal structure of AMS for competitive reasons; however, it answered questions on a more general level in a letter to the Centre for Research on Multinational Corporations (SOMO). A draft version of the report was sent to AMS, EMD, Superunie and Ahold,

Table 1 **The six largest international buying groups in Europe**

Buying group	Membership	Geographical coverage	Main focus of joint sourcing projects	Potential consumer turnover	Points of sale numbers
EMD Founded in 1989, based in Switzerland	21 members: Asda, Tuko Logistics, Superunie, Axfood, Markant Germany, Markant Czech Republic , Markant Switzerland, Markant Slovakia, Markant Austria, Casino, Dagrofa, Globus Russia, Euromadi Iberica, ESD Italia, EuromadiPort, Unil/Norges Gruppen, EMC Distributions, Kaufland Poland, Kaufland Croatia, Kaufland Romania, Kaufland Bulgaria, Woolworths.	22 countries* 	Private label products ** Not shown in map: New Zealand and Australia*	178 bn. Euro (216 bn. Euro worldwide)	150.000 stores (including sub-members, excluding New-Zealand and Australia)
Coopernic Foundend in 2006, based in Germany	4 members: Coop Italia, Ahold Delhaize, Leclerc, Rewe. It temporarily changed into "Core" which excluded Leclerc (and including Colruyt and Conad)	21 countries 	International brands. Also helping members to cooperate on private labels	142 bn. Euro	28.500 stores
Alidis / Agecore Founded in in 2002, based in Switzerland	6 members: Eroski, Edeka, Intermarché, Colruyt, Conad and Coop Switzerland	8 countries 	International brands	140 bn. Euro	21.800 stores
Eurauchan Established in 1996, in 2014 it became an international group	3 members: Auchan, Système U, Metro Cash & Carry	26 countries* 	International and national brands ** Not shown in map: China, India, Japan, Kazakhstan, Pakistan, Taiwan*	131 bn. Euro	7.300 stores
AMS Sourcing Founded in 1987, based in the Netherlands	10 members: Ahold Delhaize, Booker, Dansk Supermarked, Hagar, ICA, Jerónimo Martins, Kesko, Migros, Morrisons, Uniarme	21 countries 	Private label products for members and the Euro Shopper range	103 bn. Euro	15.000 stores
BIGS Founded in 1991, based in the Netherlands	SPAR franchise holders in Austria, Belgium, Czech Republic, Denmark, Eire, Finland, Greece, Hungary, Italy, Netherlands, Slovenia, Switzerland and the UK	11 countries 	International brands and limited to a range of approxi-mately 400 standardized own-brand products	21 bn. Euro	7.700 stores

Source: IGD Research (2016) and IBG websites (March 2017). Figures include European countries only.

all of which were given the opportunity to make comments and corrections on the draft briefing paper. All respondents participated in the review; where relevant, their comments and suggestions for correcting and improving the paper have been incorporated into the final version.

Main characteristics of IBGs

The first national buying groups in Europe date back to the 1930s. Since the 1980s and 1990s, buying groups have developed into larger and international alliances.[17] Essentially, buying groups are retail purchasing alliances that bundle procurement to improve the bargaining position and the competitiveness of their members. They come in all shapes and sizes: from informal bilateral cooperation[18] to formal organisations with their own legal and commercial identity funded through membership fees. Some are relatively open about their activities (such as EMD and AMS), while others do not even have a website. IBGs can represent small retailers or two or more larger retailers, or a combination of both. IBGs make up a special form of retail buying groups because they form cross-border alliances of retailers. Arrangements of IBGs tend to be confidential and information on IBGs is not always available.

The six leading IBGs in Europe

Table 1 lists the six largest known IBGs based on the estimated aggregated turnover of their members. The list is based on information provided by the Institute of Grocery Distribution (IGD). Apart from the market share (demonstrated by the *potential consumer turnover* of all the groups' members) and the focus of joint sourcing projects on either private label or branded products, the table shows that IBGs differ considerably in geographical coverage, while membership size varies between three and 15 participants. Also it seems that the number of participants is not directly correlated with a higher potential consumer turnover or broader geographical coverage.

The cross-border alliances usually have only one member per country to ensure that members are not direct competitors in the respective national retail markets. Thereby retailers avoid the impression of engaging in collusive practices, or overstepping market share thresholds set by national competition authorities or the European Commission, the supranational competition authority at EU level.

Some IBGs have national buying groups as their members (such as EMD). Wholesalers are sometimes also part of IBGs. They can facilitate a wider market access by selling goods to different supermarkets in a specific country, and play an important role in distributing private label products of IBGs.

Modest-sized giants

When comparing potential consumer turnover figures with the turnover of the largest individual retailers in Europe, it becomes clear that – with one exception – the retailers are outranked by IBGs in size (see Table 2). However, in practice the impact of IBGs on the European retail market is smaller than that of the largest retailers in Europe, because the volumes sourced through IBGs represent only a limited share of their members' total procurement. It is estimated that no more than 5 per cent of the total volume of individual retail members is purchased through buying groups.[19] Indeed, not all members take part in all joint buying projects and IBGs do not source the full range of products that their members stock (see following sections).

Table 2 **Largest food retailers in Europe, turnover for 2015 in Billion €, e = estimate**

Rank	Retailer	Country	Turnover
1	Schwarz (Lidl and Kaufland)	Germany	80+
2	Tesco	UK	72
3	Metro	Germany	56
4	Carrefour	France	56
5	Ahold Delhaize	Netherlands	54,2
6	Aldi	Germany	52 e
7	Edeka	Germany	52
8	Rewe	Germany	51
9	Auchan	France	49 e
10	E.Leclerc	France	44

Source: Retail Index – Worldwide figures

Six of the largest retailers in Europe are IBG members

Of the top ten largest food retailers in Europe (see Table 2), six are members of the six largest IBGs: Kaufland, Metro, Ahold Delhaize, Edeka, Rewe and Auchan. However, not all retailers are part of IBGs. The other four retailers in the top ten list – Lidl, Carrefour, Tesco and Aldi – prefer to stay 'single'. Of this group, at least Aldi and Lidl can be considered an IBG on their own: they both operate in many European countries and are known to centralise their procurement internationally to a large extent.[20]

It is not exactly clear why Lidl, Carrefour, Tesco and Aldi have not joined IBGs. One reason could be that they have sufficient leverage on their own when negotiating with suppliers, without having to compromise regional and cultural differences that sometimes prevail in buying groups.[21] Another reason could be that they prefer not to share information about suppliers to remain competitive vis-à-vis other members.[22]

Membership dynamics

Joining an IBG is simple and attractive as it requires little investment in terms of cash or management resources. The cost of running the group operation is shared by all members and operating surpluses are returned to them. Usually, a candidate needs to be approved by the existing members before joining a buying group.[23]

In terms of stability, there are significant differences between the six largest buying groups. Although information about membership size and composition over time is difficult to gauge from public sources, some buying groups (like EMD and Alidis/Agecore) have been highly stable, while others expanded, such as AMS, or decreased.[24] Other groups seem to be in flux with retailers switching from one buying group to another. For example:

- Delhaize announced a shift from AMS to Coopernic in September 2014, but returned to AMS in June 2015. After the merger, the new company Ahold Delhaize decided to stay/become a member of both AMS (in order to support buying private label ranges) and Coopernic (to drive procurement of branded products).[25]
- Système U changed its membership three times: first, it left AMS for Core in May 2014. Shortly afterwards, Système U and Auchan jointly formed Eurauchan, together with Metro.
- Rewe, Colruyt, Coop Switzerland and Conad founded Core (and left Coopernic) in 2014. However, Rewe decided to return to Coopernic in June 2015.[26]

The Ahold Delhaize merger marks the first time a retailer has become a member of two separate IBGs. This could improve the information position of these IBGs as information (on prices) can be exchanged between the two more easily.[27] The many changes in membership suggest that retailers are continuously re-considering the benefits of membership and are looking for the best platform to achieve buying synergies.

Product focus

The main focus of IBGs in Europe is on products that cater for uniform and widespread consumer preference in different countries with a long shelf life. These include international brands and mainstream products like flour, olive oil, sugar, rice, pasta, tomato paste, canned tomatoes and other canned vegetables.[28] In this category, international buying groups are most succesful in obtaining benefits and discounts from suppliers (Chapter 4 explains this in greater detail; see also Boxes 3 and 4 for examples of specific products – orange juice and sweet biscuits – that are sourced through IBGs). Fresh fruit and vegetables, as well as products with a short expiry date, are generally not bought collectively.[29]

Box 2 **Development of private labels**

The development of private labels is a key competitive strategy among retailers. With private labels, stores can be distinctive and accentuate or create their identity. Private label products allow retailers to determine how products look and taste. These products are often sold at a lower price than branded products, because their marketing and development costs tend to be lower.

From the perspective of brand manufacturers, supermarkets are thus not only clients but also competitors. Their products compete with supermarkets' private label products, not only on the basis of price but also visibility. Brand manufacturers are usually charged for a visible product placement and for in-store promotion. Competition from supermarkets' private label brands may be even fiercer when supermarkets increase promotion for private label products simultaneously with, or ahead of, the promotion campaigns of branded goods.[30] Retailers often have access to, or require information, on product development or promotion plans of brand suppliers, which gives them a privileged position.

Europe has a high average market share for private labels of 36 per cent.[31] Across Europe, market shares vary from 45 per cent in Switzerland to 16 per cent in Greece (see also Box 3 and 4 for private label share in the sweet biscuits and orange juice sector).[32] Estimates suggest that the market share of private labels in Europe will reach 50 per cent by 2025.[33] Private label products are particularly strong contenders in product groups where there is only little difference between products with regard to specific features or packaging.[34]

Retailers often choose to offer private label products in three ranges: economy products (low budget), standard products and premium products. In the economy segment, profit margins may be very low compared to premium and standard segments. By catering to consumers in all three ranges retailers not only secure profits but also compete more effectively with brand products.[35]

IBGs tend to focus strategically on the procurement of either private label or branded products. Alliances like Alidis/Agecore, Coopernic and Eurauchan focus on improved sourcing terms for branded products (see also Table 1). By contrast, EMD and AMS both focus on the sourcing of private labels only. See Box 2 for more information on the supermarket private label strategy.

The procurement process

The sourcing of products within IBGs typically starts with an (online) meeting where members discuss which items to source collectively. This is followed by a decision about which suppliers to invite and how to harmonise the specifications of the chosen product. Selected candidates will then be invited to make a bid and are asked to disclose detailed information about the product and price. Normally, the step of quoting takes place in online buying systems or electronic auctions. After selecting a supplier and negotiating on prices and other terms such as the volume, the group draws up an umbrella contract. The buying group does not make purchases collectively, but individual members contract the supplier under the terms of this umbrella contract. Individual members usually make all other arrangements regarding transport, packaging or promotional activities with the supplier.[36] More detailed information on the procurement process of the international buying groups AMS and EMD will be provided in the next section. As there is no information available on the procurement processes of IBGs with a focus on premium brands, it is difficult to assess whether these processes are different.

In focus: Two large private label IBGs

For a better understanding of retailers' internationally combined buying practices and possible effects on the relationship between supermarkets and suppliers, this section looks more closely at how two prominent IBGs work: EMD and AMS – the two oldest alliances with far more members than others, which are well-known for buying private label products – a key competitive strategy for retailers.

EMD: a group of groups

Legal status:	Private company
Registered as:	Purchasing and marketing organisation
Employees:	17
Turnover:	€ 4.1 m (estimate for 2014)[37]
Ownership:	All members are shareholders
Management:	Board of directors (six) from five different retailers and one managing director[38] European Marketing

Distribution (EMD) was founded in 1989 in Switzerland. EMD started as an initiative of smaller retailers that sought to compete with larger ones. Currently, the buying group has 21 members: Asda, Tuko Logistics, Superunie, Axfood, Markant in five countries, Casino, Dagrofa, Globus Russia, Euromadi Iberica, ESD Italia, EuromadiPort, Unil/Norges Gruppen, EMC Distributions and Kaufland in four countries. Australian retailer Woolworths joined in March 2017.

Although EMD includes individual retailers as members, most of them represent national-level alliances of smaller supermarket chains. For example, ESD Italia purchases for a group of five independent retailers in Italy; Euromadi purchases for retailers in Portugal and Spain; and Superunie buys for 13 smaller supermarket chains in the Netherlands.

Apart from joint buying of private label products, EMD performs two other types of activities: it engages in paid marketing activities for premium brand suppliers, which can be rolled out in different countries simultaneously, and offer brand suppliers a European platform for trade and marketing. Furthermore, EMD offers a network for suppliers on the basis of which suppliers are introduced to retailers without them having to initiate meetings. If these meetings lead to a contract between the supplier and one or more EMD members, EMD receives a commission.[39]

EMD works with annual product sourcing plans for private label products, like rice, ice tea and beer. Currently, EMD is running about 70 projects (food and non-food) of which the joint buying of sodas is the biggest with a volume of 50 million litres per contract. Other larger and more frequent EMD projects include: pasta (about 34,000 tonnes per contract); and deep frozen potato (with an estimated 20,000 tonnes per contract).[40] EMD offers about 39 categories of private label products. The majority of these are marketed as the specific brand 'Eurolabels', for which the trademark rights are held by EMD.There are currently over 200 different Eurolabel products available to members.[41]

The sourcing of a certain product starts with the forming of a working group that selects suppliers and formulates specifications. All members that wish to be involved can usually participate. A working group takes the lead and consists of so-called 'expert buyers' from individual members. Within the working group, information on suppliers is shared freely. The number of participants varies within each product/working group; members might even withdraw during the specification phase. EMD facilitates and prepares the tender procedure. As soon as specifications are formulated, a *Request for Information* is send to all potential suppliers. This document contains specifications referring to packaging, quality requirements, supply chain information, and/or sustainability desires. Suppliers can express their interest by email. The working group selects five to ten applicants (out of up to 100 companies) and sends out a *Request for Prices*, which is followed by negotiations and the signing of an umbrella contract with the selected supplier. This is an agreement on price and quantity only. Once an order is placed, the members of the working group can buy under the umbrella contract, with individual members negotiating packaging and transportation directly with the supplier.

Contracts with suppliers usually run for a year, sometimes six months. The buying group states that it cares about having small- and medium-sized enterprises (SMEs) in its supplier portfolio, but acknowledges that, in practice, only large suppliers are able to deal with the required volumes. According to EMD, suppliers are often long-term partners. EMD also claims to source only products of the highest quality and sustainability norms as required by individual members (such as, for example, specified in the Superunie code of conduct)[42] for the whole tender. EMD states it does not need an overall code of conduct, since the actual buying takes place at individual retailer level.

AMS: Known for its Euro Shopper products

Legal status:	Private company
Registered as:	Market research organisation
Employees:	38 (most of them are buyers)
Turnover:	€ 6 m in 2014[43]
Ownership:	7 members are shareholders
Management:	Management Team of 4 and a managing director reporting to AMS Supervisory Board

Associated Marketing Services (AMS), or AMS Sourcing, started in 1988 in Switzerland with three members. The group's 10 current members are Ahold Delhaize, Booker, Dansk Supermarked, Hagar, ICA, Jerónimo Martins, Kesko, Migros, Morrisons and Uniarme. Some members act as wholesalers or distributers in their domestic market (for example, Booker in the UK), providing a wider market for AMS-sourced products. Through its members, AMS is active in 21 European countries. In 2006, headquarters were moved from Switzerland to the Netherlands.

AMS initiates, manages and coordinates joint buying activities for its members through an online interface called Marketplace (introduced in 2005). Possible suppliers are contacted to send in quotes to AMS. AMS staff then analyse these quotations, based on the specifications required by its members. Once suppliers are selected, they negotiate, agree and sign an umbrella contract with AMS.

Once signed, this umbrella contract is transferred to individual AMS members, who then take care of ordering, packaging, paying and logistics.[44]

AMS is primarily a food grocery buying group, with only a small share in bundling non-food product sourcing. The vast majority of AMS's business is focussed on sourcing private label products, such as Euro Shopper label products. The Euro Shopper brand covers approximately 300 food and non-food products, which are marketed exclusively by AMS and distributed in seven European countries.[45] The products from the Euro Shopper range are available to all members, although some members have chosen to discontinue this AMS label in favour of their own private label economy products. This was the case with Ahold in 2013, AMS's largest member in terms of sales. Ahold's decision had a very significant impact on the market share of Euro Shopper, since Ahold accounted for half of the range's volume.[46]

AMS works with suppliers from across Europe. It prides itself on its long-established core of suppliers, and the reliability in terms of service and quality that these relationships bring to their members. This allows the buying group to source across all product categories and to align product specifics as much as possible with the individual preferences of members. New members bring in new suppliers, which broaden the sourcing base. Most products are sourced in Europe, but since 2010 AMS has also been expanding its joint sourcing efforts in Asia.[47] Decisions about which products should be subject to joint buying are taken by AMS members.

According to the Dutch retailer Albert Heijn (part of Ahold Delhaize), AMS suppliers operate both nationally and internationally. Bidding suppliers are informed about which retailers will be involved in the tendering project. How often tenders are issued for certain products depends on the product, harvest time and market situation. Albert Heijn states that the negotiations of AMS take place in face-to-face meetings or via phone calls.

Albert Heijn also points out that sustainability issues are important to both AMS and Ahold. AMS is committed to sharing knowledge between partners on sustainability and organises annual meetings on this subject.[48] Contracts agreed on behalf of Albert Heijn should comply with the Ahold code of conduct.[49] AMS does not have its own code of conduct, but applies the different codes of conduct of its members, where relevant in the sourcing process.

IBGs' leverage on suppliers

In order to understand the dynamics between IBGs and suppliers, it is useful to make a distinction between downstream factors, related to the position of retailers, and upstream factors, related to the position of suppliers and manufacturers, affecting the terms of trade. Examples of downstream factors are the retailer's market share (retailer power), their information position and their ability to influence the terms of trade with upstream suppliers (buyer power).[50] Examples of upstream factors are the type of market in which manufacturers operate, the capacity and scale of production of manufacturers, the distinctiveness of the product and the ability to offer added value. Both types of factors have an effect on the power relation between IBGs and suppliers.

Downstream factors: IBGs' ability to increase buying power

The section on 'Main characteristics of IBGs' shows how the aggregate turnover of a group's members underpins the retailer power of IBGs, which fosters their negotiating position to determine the terms of trade with upstream suppliers. Another way IBGs can increase their leverage on suppliers is by exchanging information internally and comparing prices from bidding suppliers. Some suppliers think this one-sided information-sharing affects them in a negative way. One producer manufacturing both brand and private label interviewed for this research said: "I do not want to sell through a buying group, because of the risk of such operational information being used in negotiations, or shared with, individual retailers, who can potentially use the information to enforce lower costs in current contracts"[51] Suppliers prefer not to provide sensitive information that can be shared between (potential) clients; however, they often have no other choice as they are dependent on the retailers. The fact that suppliers do actually comply with such demands is telling of the fierce competition and asymmetric power relations in the grocery supply chain. Mostly only large suppliers are able to deal with the required volumes.[52] This might crowd out smaller players by which IBGs directly or indirectly spur further consolidation of supplier markets.

Because IBGs source across different countries, suppliers not only face competition nationally but also internationally. This results in intensified competition among suppliers and creates additional leverage for IBGs to secure better deals.[53] On the other hand doing business with IBGs offers certain advantages for suppliers. In addition to potentially increasing sales volumes, it may provide access to new clients and new national markets, all of which allow for economies of scale and opportunities for further investments or innovation.[54]

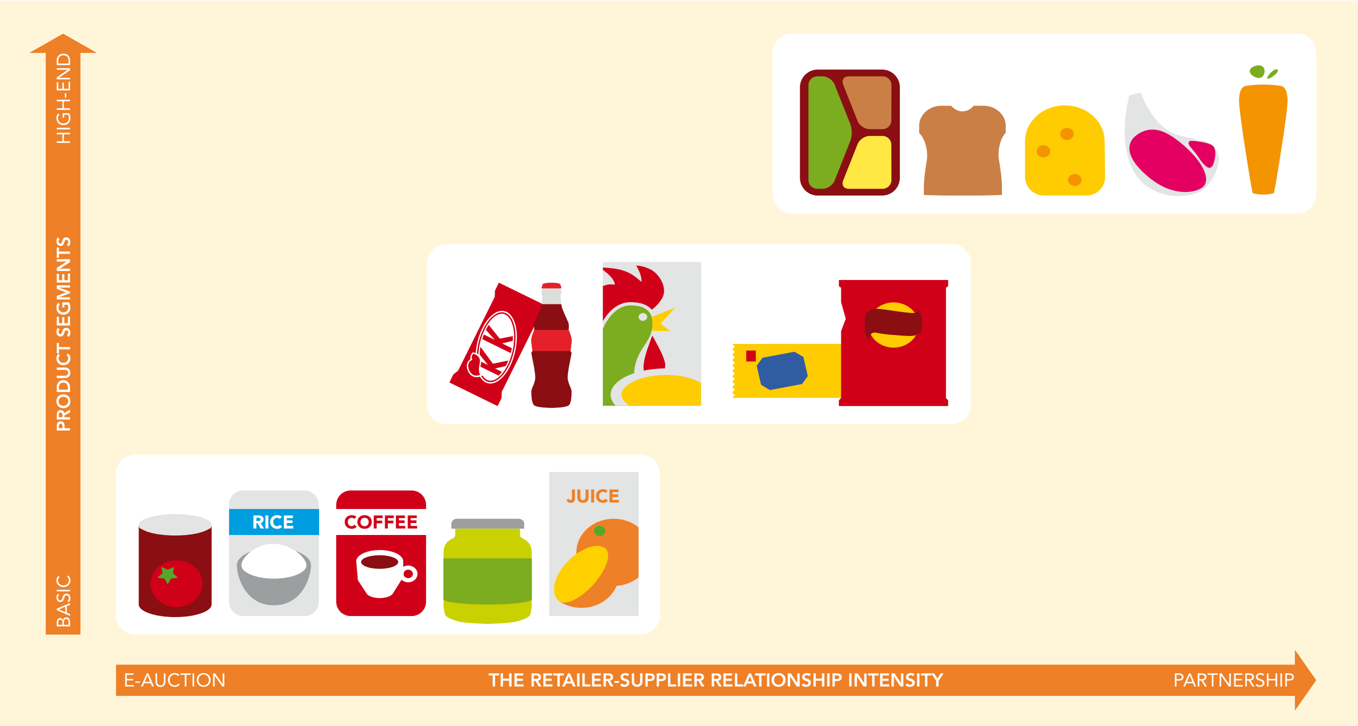
Finally, the opportunity for IBGs to negotiate lower prices with suppliers depends on the ability to align buying projects and product requirements. If the required product is fairly uniform, it can be easily produced in large quantities. Moreover, if commodity prices are stable and if all participating retailers require more or less the same specifications, significant discounts can be negotiated with suppliers. Estimates suggest in such cases, products can be sourced at a 5 to 10 per cent[55] discount compared to the price individual members would pay.

Upstream factors: different levels of bargaining power for suppliers

Various upstream factors may have an effect on supplier bargaining power, too. Supermarket products can be categorised into different segments, each defining a different type of relationship between retailer and supplier.[56] Figure 2 shows two variables. The vertical axis indicates the level of product differentiation and discerns three different segments: basic, brand and exclusive products. The horizontal axis indicates the level of closeness of the retailer-supplier relationship, which is directly influenced by the upstream factors in the vertical axis. On this axis three levels can be discerned as well, varying from anonymous e-auction systems with limited bargaining power for suppliers to long-standing partnerships between retailers and suppliers. More seller power for suppliers does not automatically translate in more amicable relations or friendly negotiations.

In the first segment, at the top of Figure 2, are products that are essential to the perceived quality of the supermarket including fresh fruit, meats, cheeses and vegetables, as well as high-end exclusive products (private label examples include Albert Heijn's 'Excellent' or Tesco's 'finest' ranges). These products have a strategic role in positioning the supermarket. Manufacturers of these high-end products offer added value to customers and thereby help retailers to be distinctive and accentuate their identity. As a result, retailer-supplier relationships are often long-standing and relatively stable.[57] Margins of these suppliers tend to be potentially higher than those for suppliers in more flexible arrangements. However, this does not mean that margins for suppliers in this product segment are necessarily good or without downward competitive pressures. Recently, a Dutch fruit trader complained about the heavy price pressures exerted by Albert Heijn.[58] IBGs are usually not active in this segment because product specifications tend to be too diverse, and also the shelf life may be too short for the procurement process of IBGs.

Figure 2 **Differentiating strategies of retailers with corresponding relation with suppliers**



Source: SOMO adopted from Rabobank

The second group includes products that customers expect in every supermarket such as premium brand products from suppliers like Nestlé, Unilever or Coca-Cola. As most retailers consider stocking certain premium and household name branded products as essential for their business, this relationship is defined by a certain level of interdependence between the retailer and supplier. Suppliers of branded products usually have a better bargaining position with retailers than those selling private label (the third group). Moreover, premium brand manufacturers are often large multinational players in the food sector (to illustrate Nestlé's turnover in 2015 amounted to €82.8bn[59] and Unilever's to €53.3bn[60]), which provides these companies with a better bargaining position than smaller competitors. Nevertheless, every detail, ranging from shelf position to selling prices, is subject to annual negotiations. The negotiations have been reported as tough[61] and conflictive, often including threats or actual refusals by retailers to supply certain products in their stores.[62] Some IBGs in Europe are active in this product segment.

The third category of products consists of interchangeable, private label products. The procurement process often takes place in online buying systems or online auctions where the lowest price offered wins the contract. Suppliers in this segment usually have limited bargaining power and operate in a highly competitive market. From the perspective of private label manufacturers, they are being played off against one another. There is a constant looming threat for suppliers that the contract might be awarded to cheaper competitors. Indeed, sometimes suppliers are forced to sell at a loss, just to keep their clients on board.[63] The limited bargaining power of private label manufacturers is also evident from the high level of transparency that is required from them in their dealings with clients. Private label manufacturers typically need to disclose detailed information on the costs of their production.[64] Therefore retailers have a detailed insight into the cost price of the product, revealing specific information on prices paid for raw materials and packaging, as well as the manufacturing costs. One manufacturer interviewed for this research revealed that, in online buying systems of retailers, applicants have to disclose details about capacity, machines, factories, net profits and volumes.[65] However, this segment is also characterised by large differences in upstream factors. One expert states that a large majority of the (private label) manufacturers are perfectly capable of maintaining a good position and generate good margins by being distinctive and provide for products with high added value.[66] On the other hand, Boxes 3 and 4 give details about two very different market structures: the fragmented biscuits market and the consolidated orange juice market; despite the differences, manufacturers in both markets face fierce price pressure from retailers. IBGs focussing on private label products are active and, as stated before, are the most successful in negotiating lower prices with suppliers in this segment.

Box 3 **Sweet biscuits – a fragmented market**

Biscuits are subject to different national tastes and preferences. This makes it difficult for retailers to source biscuits through IBGs. Only types of biscuits that are well known internationally are being sourced this way, like premium brand biscuits, chocolate chip, wholemeal and fourré cookies.

Sales in the Western European biscuit market amount to €12bn annually.[67] The market is highly competitive and fragmented, with over 50 larger biscuit companies fighting for the biggest market share. Often, producers bake for both brands and private labels. Parallel to trends in other sectors supplying retail and indeed retail itself, the biscuit sector is characterised by increased concentration[68] in which private equity has also started to play a role.[69]

The share of private labels in sweet biscuits was 25 per cent in 2015 in Europe as a whole, with large national differences (Germany 46 per cent; Estonia 4.6 per cent).[70] The largest brand companies active in the Western European market are: Mondelez, United Biscuits, Barilla, Bahlsen and Yildiz. Well-known private label manufacturers include: Continental Bakeries, Griesson-de Beukelaer and Groupe Poult.

The leading chocolate chip cookie manufacturer is Merba, while Pally Biscuits is one of the biggest dry biscuits producers.[71] There are also many smaller, family-owned businesses with a more local focus.[72]

European biscuit manufacturers experience severe pressure from large retailers.[73] Price agreements with retailers are typically set for 12 months, whereas commodity prices for flour, cereals, chocolate, nuts and palm oil fluctuate on a daily basis. As retailers typically display little flexibility when it comes to renegotiating price agreements in the interest of suppliers, this leaves biscuit companies exposed to uncertainty and constantly changing margins.

This is not the only reason biscuit producers are sometimes reluctant to enter into contracts with buying groups. Some manufacturers interviewed for this research stated that they need to reveal too much information on prices, capacity and their own profit margins. Also, the complexity of different contracts with national retailers under one umbrella contract with the international buying group is reported to be too complex for many (smaller) producers.[74]

Box 4 **(Orange) juice – a concentrated market**

(Orange) juice is a fairly uniform product, which makes it easy to source in very large quantities and therefore straightforward for IBGs to manage. 'Juices'[75] represent one of the biggest buying projects for EMD, which handles about 40 million litres annually.[76] This represents a modest 0.6 per cent of the 6.2 billion litres of the total EU fruit juice consumption in 2014.[77]

The European juice sector is less fragmented than that of biscuits; in 2010 there were a total of 35 European bottling companies.[78] Total production of fruit juices in the EU was worth €6.4bn in 2014.[79] Most orange juice is produced from concentrate. Over half of the orange juice concentrate supply in Europe is imported from Brazil. Three orange juice processing multinationals (Louis Dreyfus Company, Cutrale and Citrosuco) control the global market and generally supply over 50 per cent of all worldwide bottling companies.

The share of private labels in the European orange juice market was 25 per cent in 2015, with large national differences (Germany 48.2 per cent; Bulgaria 1.2 per cent).[80] In Germany, the third largest retailer, Edeka, even acquired four production units for fruit juice. Refresco-Gerber is the leading European private label bottler.Large juice brands are: PepsiCo (Tropicana, Punica) and Coca-Cola (Minute Maid, Innocent and Oasis).[81]

Bottlers are in a tight position between their powerful suppliers of orange juice concentrate on the one hand and their powerful clients on the other hand. In its annual report, Refresco-Gerber, itself the result of recent merger,[82] states that: "Most of our customers are large and sophisticated retailers and premium brand owners which, as a result of their size, have significant buying power and can often apply pricing pressure."[83]

Possible market impacts of IBGs

Apart from the ability of IBGs to obtain more favourable conditions from suppliers than their individual members would, they may have a number of other impacts on the market as well.

Higher risk of exposure to unfair trading practices

IBGs have not been accused publicly of unfair trading practices but this does not mean that suppliers dealing with these groups do not experience them. Indeed, as well as the generally high prevalence of UTPs in this sector as a whole, the fear of retaliation in the absence of effective sanctions typically prevents victims of UTPs from going public with their grievances (also see Box 5).[84] However, when looking at the structural characteristics of IBGs, it becomes evident that they are creating conditions that may facilitate the occurrence of UTPs. In particular, the way terms are negotiated and contracts are concluded within IBGs increases the risks for supplier exposure to UTPs.

As noted at the beginning of this paper, suppliers that are successful in winning an IBG project are offered an umbrella contract. If at the end of the road the price or volume is different from what was contractually agreed on this would constitute a UTP. On this level the risk of UTPs from IBGs may be similar to that of the supplier dealing with a large supermarket directly on volume and price. However, in contrast to bilateral negotiations, the supplier to an IBG then still needs to negotiate all other terms in contracts with all the individual retailers within the buying group's project. As there is a risk of encountering UTPs in commercial relations with each individual member, the risk of exposure to UTPs is logically higher in a number of consecutive bilateral negotiations than in just one.

There is at least one other way by which IBGs may facilitate UTPs. As noted earlier, suppliers for private label products may need to be transparent about their costs and sometimes even their excess capacity and production process in the initial negotiations and/or bidding with IBGs. Such demands, that can erode a supplier's competitive position, can already be qualified as excessive and hence as UTPs.[85] However, these demands do not present a new and/or necessarily higher risk as such: suppliers may be confronted with similar demands in ordinary (bilateral) negotiations. In contrast, the risk of commercially sensitive information being shared internally among IBG members is both a new and higher risk. IBGs represent groups of retailers by definition, and this provides them with a platform for information exchange. Both these factors also expose

Box 5 Unfair trading practices

UTPs come in many forms[86] but the most prevalent are non-respect of contractual terms such as delays in payment, threats of delisting when a supplier refuses to comply with unjustified advantages such as lower prices, and unilateral deductions on invoices without sound business reasons.[87]

UTPs are typically imposed by a stronger party on a weaker one in a situation of imbalance. Unfair trading practices (UTPs) occur in many sectors but they are especially prevalent in the food supply chain.[88] Research commissioned by European food and drink industry organisations in 15 European countries, involving more than 680 brand and private label manufacturers, showed that practically all companies (96 per cent) experienced UTPs in 2009.[89] Specific cases that received media attention recently include: Ahold Delhaize, which was accused of demanding unfair concessions from its largest suppliers in the Benelux countries; Carrefour, being taken to court by the French government for seeking discounts from suppliers illegally;[90] and Tesco, facing investigations of the groceries code adjudicator on delayed payments to suppliers.[91]

The fear that client retaliation may seriously affect their business makes victims of UTPs weary of complaining publicly or openly with authorities. This is one reason why contract law, for example, cannot deal effectively with UTPs. Similarly, because perpetrators of UTPs usually do not have a dominant market position, competition law is also largely inadequate in tackling UTPs. The proliferation of UTPs in a context of inadequate regulatory instruments, has led 20 EU member states to introduce specific legislation to address UTPs of which 15 countries over the last five years.[92] Meanwhile two European Parliamentary motions calling for a European level regulatory framework of UTPs have not convinced the European Commission to take action.[93] To effectively address UTPs being applied across borders, as may be the case in IBG procurement relations, this is a major hindrance.

suppliers to a higher risk of this information being abused in future negotiations directly, and indirectly, in the event this information finds its way through members to the competing suppliers.[94] With the newly formed retail giant Ahold Delhaize being active in two different buying groups, this risk is even expanded to include commercially sensitive information being exchanged between IBGs instead of only within IBGs. See box 5 for EU policy approaches to countering UTPs.

In response to a draft of this research, the Dutch retailer Ahold and the Dutch national buying group Superunie claim not to recognise the asymmetrical relationship between suppliers and supermarkets, nor the possible UTPs resulting from this. They argue that relationships are much more interdependent than is suggested in this briefing, that innovation and sustainability are pillars of their long-term success and that UTPs are not.[95] EMD notes that potential UTPs on the level of individual members, such as unfair payment requirements, would be a reason to exclude these members from future projects because it compromises the position of other members that honour the terms of the joint umbrella contract.[96]

Anti-competitive effects?

A number of issues that this report finds in relation to IBGs may impact markets negatively but need not, or cannot, be discussed in the context of UTPs only. Could competition law be used as an instrument to address these issues?

Competition authorities in Europe are active in monitoring and regulating the retail sector nationally. They do this on various levels, for example, in cases of mergers and also on different forms of cooperation including on national buying alliances.[97] Also the European Commission is active in scrutinizing retail mergers all over Europe.[98] However, to date there is no evidence of national or European level competition investigations in IBGs. Competition authorities apparently do not have IBGs on their radar yet. It is unclear to what extent existing EU competition laws and enforcement are equipped to address IBGs and their harmful effects.

This report shows that IBGs are able to increase the buying power of their members considerably. Through downward price pressure this (momentarily) manifestation of higher retail concentration may impact negatively on suppliers and conditions for workers further down the supply chain. As long as consumers benefit from the lower resulting prices, manifestations of market concentration - in the form of more or less permanent corporate alliances such as IBGs, or other forms - hitherto seem permitted under current competition law.[99]

This primacy given to lower prices at the expense of potentially harmful and abusive market power concentration reflects the narrow focus of competition law. Also the desired consumer welfare enhancement remains questionable, as there is no evidence or assurance that lower prices extracted from pressuring suppliers is indeed passed onto consumers.

The narrow view ignores moreover that IBGs can be an obstacle for market access for smaller suppliers. The one-sided terms of trade, where suppliers have to provide access to business sensitive information, allows IBGs to share and use the information potentially inappropriately. It can be argued that such effects are undesirable even from a narrow market efficiency perspective as it may ultimately reduce innovation and diversity in the suppliers' market. However, as suppliers are supposedly free to engage with IBGs and accept their terms and required information, such IBG effects and practices continue to be perceived unproblematic by competition authorities.

Setting ethical standards?

For this briefing, the use of ethical standards by IBGs was also investigated. Both EMD and AMS do not have specific group ethical/ecological requirements for suppliers. The fact that two of the largest IBGs do not uniformly apply ethical and ecological standards suggests that other IBGs do not apply them either, although this cannot be verified due to a total lack of public information on other IBGs. However, both EMD and AMS claim that the member in a buying project with the highest sustainability requirements effectively sets the standard for the project as a whole. Hence from the perspective of markets of the IBG members with the lowest procurement standards, IBGs potentially could have beneficial effects. It should be noted, however, that higher sustainability requirements do not automatically translate into better conditions at suppliers especially if assured inadequately. Hence in practice beneficial effects (if any) may be limited when the standard setting member has no proper implementation system at group level.

Also the IBGs focus on achieving lower prices than individual members would pay could jeopardise the potential beneficial effects of sustainability requirements. A general complaint of suppliers is that, when retailers require sustainability conditions, they are not always willing to implement pricing and delivery terms that allow ensuring compliance with social and environmental standards.[100] If such enabling factors are not ensured, suppliers will need to absorb extra costs and efforts or pass them on to their suppliers further down the supply chain.

Conclusions

Many leading European grocery retailers – including Kaufland, Metro, Ahold Delhaize, Edeka and Rewe – are increasing their leverage on suppliers through international cooperation and bundling volumes. At least six IBGs operate on a European level; their main aim is to combine procurement in order to get discounts. Especially basic (private label) products that are uniform and can be bought in bulk lend themselves to joint procurement: IBGs may negotiate discounts as high a 10 per cent, compared to the price an individual retailer would have to pay. The opportunity for IBGs to negotiate these levels of discounts depends not only on the type of product and the (often limited) bargaining power of suppliers but also on the ability of IBGs to align buying projects and product requirements. If they succeed in aligning buying projects, IBGs can make use of their retailer power: they have a potential consumer turnover that outranks leading individual retailers in Europe.

Doing business with IBGs offers suppliers certain advantages. In addition to potentially increasing sales volumes, it may give access to new clients and new national markets – all of which allow for economies of scale and opportunities for further investments or innovation. However, suppliers that want to qualify for IBG tenders can expect a bumpy ride. First, they are competing internationally with many other suppliers to get a contract, and then they have to reveal detailed information often including details on margins, capacity and future planning in quotes to retailers. The supplier with the best offer negotiates price and volume with the IBG, resulting in a so-called umbrella contract. After that, the selected suppliers need to negotiate all other details, including packaging and transportation, with all the interested IBG members to secure individual contracts with them.

Although there is a high prevalence of unfair trading practices (UTPs) in the retail sector and IBGs have not been connected to them directly, IBGs create conditions that facilitate the occurrence of UTPs. The umbrella contract system with extra rounds of negotiations on additional conditions with individual IBG members can lead to unforeseen costs for suppliers. Also logically the risk of supplier exposure to UTPs is higher in a number of consecutive bilateral negotiations than in just one. Another way by which IBGs may facilitate UTPs is the level of transparency that may be imposed on them.

Suppliers disclosing commercially sensitive information may be shared internally among IBG members and exposes suppliers to a higher risk of this information being abused in future negotiations directly, and indirectly, in the event this information finds its way through members to the competing suppliers.

IBGs do their work behind the scenes without the general public being aware of them. The fact that IBGs create conditions that may facilitate UTPs should be an important focus of the coordinated European approach to tackle unfair practices in the food supply chain that the European Parliament calls for. IBGs should use the full potential of their leverage to jointly strengthen the requirements on sustainability and put primary producers and workers at the core of their negotiations, instead of just the lowest price for their members.

The scale of the procurement handled by IBGs, and the high level of sharing supplier information temporarily creating a disproportionally large market share, raises questions about how such an economic power amalgamation relates to competition law. It seems that competition law in its current form in Europe is not equipped to address IBGs or resulting possible negative market impacts. Although national competition authorities and the European Commission put much emphasis on price competition as a way to increase ‘consumer welfare’, whether the joint negotiation by IBG members indeed result in lower prices for consumers seems beyond the realm of investigations into abusive practices.

The role that IBGs play in supermarket strategies to lower procurement prices and the negative effect this may have on conditions for suppliers and workers further upstream, should receive more attention from EU policy-makers and competition authorities in particular. Because of their complex and obscure nature and a lack of effective policy instruments, a tailored EU policy framework may be required to address this phenomenon.

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Colophon

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