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Competition in the Food Supply Chain – Contribution from Portugal

- Session IV -

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More documentation related to this discussion can be found at: oe.cd/gfc24.

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Competition in the Food Supply Chain

- Contribution from Portugal –

1. Introduction

1. In Portugal, in the peak of food inflation which occurred in February 2023, the index for unprocessed food products recorded a variation of 20.1%¹. Several factors have contributed to this sharp inflation, namely the disruption of global agricultural markets caused by the war in Ukraine, in particular regarding cereals and fertilizers, the weather conditions and the rising energy costs.
2. This context has put significant pressure on the purchasing power of households and has contributed to governmental support measures in Portugal.
3. During this inflationary context, the AdC actively voiced how competition policy can help protecting the purchasing power of households, with recommendations to the government and to firms, including directed at the food supply chain given its impact on the purchasing power of households.
4. In addition, the AdC has recently investigated and issued several sanctioning decisions involving food-based retail distribution companies and their common suppliers. These decisions illustrate anti-competitive practices that can occur in the food value chain.
5. The present contribution outlines insights based on both advocacy and enforcement actions conducted by the AdC related to the food supply chain.

2. Anti-competitive practices in the food supply chain

2.1. AdC's hub-and-spoke decisions in the Portuguese grocery market

6. Following a resale price maintenance (RPM) investigation² regarding a beverages' supplier and its distributors in the on-trade channel, the AdC found evidence of additional possible anticompetitive practices in the off-trade channel.
7. Therefore, between 2017 and 2023, the AdC investigated and decided several cases involving food-based retail distribution companies and their common suppliers, in markets related to diversified categories of Fast-Moving Consumer Goods (FMCG), namely beverages, packaged bread and cakes, hygiene and home care products³.
8. In 2017, the AdC conducted dawn raids in the premises of 21 legal entities. This led to 10 sanctioning decisions under Article 9 of the Portuguese Competition Act, as well as Article 101 of the Treaty on the Functioning of the European Union ("TFEU"). In sum,

¹ INE, Consumer price index, February 2023.

² On 24 July of 2019, the AdC imposed a fine of 24 million euros on the beverages' supplier for resale price maintenance ("RPM"). This decision has been upheld by the Courts.

³ Proceedings nos. 2017/01, 2017/03, 2017/04, 2017/05, 2017/06, 2017/07, 2017/08, 2017/11, 2017/12 e 2017/13, currently under judicial review, details of which can be found at: AdC - PesquisAdC (concorrenca.pt).

the decisions resulted into fines amounting to more than €690 million to six supermarket chains and ten suppliers.

9. The evidence collected demonstrated a set of bilateral vertical practices or agreements to fix the resale price, along with elements that configured a multilateral collusion between competitors, facilitated by a common supplier, commonly referred as hub-and-spoke agreements.

10. In the case of a hub-and-spoke scheme in which the hub is the common supplier and the spokes are the retailers, it is the supplier who, through a set of bilateral communications with the different retailers, facilitates, promotes and/or guarantees the illicit collusion between the companies at the bottom of the distribution chain (the retailers - spokes).

2.2. The role of grocery chain bargaining power in AdC's hub-and-spoke investigations⁴

11. A key element in a hub-and-spoke investigation with a common supplier is to understand the incentives of both retailers (i.e., grocery chains) and suppliers to participate in the collusive scheme. While the incentives for retailers to participate are more similar to those of a traditional cartel (i.e., softening price competition and obtain higher retail margins), the incentives of suppliers to participate in such arrangements are less straightforward. Indeed, a retail price above the competitive level would imply, in general, a lower volume of sales and hence, a lower revenue stream for the supplier.

12. This, however, abstracts the situation in which retailers hold bargaining power over suppliers. As such, retailers have an incentive to put pressure on suppliers as to obtain better supply offers and gain an edge downstream where they compete with other retailers. As retailers try to decrease supplier prices, this may lead to lower supplier and retail prices.

13. As highlighted by the OECD (2019)⁵, in a situation where retailers pressure a supplier to obtain low retail prices or margins, a hub-and-spoke scheme can serve as tool for a supplier to avoid a reduction in its margins.

14. Thus, a context of grocery chain bargaining power and retail market concentration may provide an alignment of incentives of all involved firms in a hub-and-spoke scheme, and it is an important element to consider in an antitrust investigation.

15. Already, in 2010, in the context of sectoral inquiry into the commercial relations between food distributors and their suppliers⁶, the AdC had concluded that, unlike traditional commerce, larger retailers concentrate a more diversified basket of FMCG, in each of their units (from food to personal hygiene and drugstore and bazaar products), and have central purchasing centres for their supplies, thus giving them greater bargaining power vis-à-vis suppliers.

⁴ For further detail on this see Rodrigues, et al “Hub-and-spoke Cases in the Portuguese Grocery Sector” CPI Antitrust Chronicle, December 2021 (available here).

⁵ OECD (2019) Roundtable on Hub-and-Spoke Arrangements – Background Note (available here).

⁶ Autoridade da Concorrência, “Final Report on the Commercial Relations between Food Distributors and their Suppliers”, October 2010 (available here, in Portuguese only). This Report was undertaken following an on-going public debate on potential unbalanced commercial relations between larger retail groups and their suppliers and increasing tensions in these relations.

2.3. AdC's advocacy action against anti-competitive practices in the consumer goods value chain

16. Following the investigations and sanctioning decisions involving hub-and-spoke arrangements in the food supply chain, in April 2023, the AdC published a paper on “*Defence of competition in times of inflation: Recommendations on the value chain of consumer goods*”⁷. This paper presents a series of recommendations aimed at raising awareness among companies along the value chain of consumer goods of the importance of adopting strategies in line with the best competition practices.

17. In particular, the AdC recommended operators in the value chain of consumer goods to periodically review their commercial behaviours to prevent risky conducts along the value chain, taking into account the following situations:

- A resale price recommendation should not eliminate companies' freedom to establish their own prices.
- Resale price maintenance and the direct or indirect exchange of strategic and commercially sensitive information is illegal, even in the promotional context.
- Margins along the value chain should not be guaranteed at the expense of price coordination between companies.
- Resale price monitoring tools should not be used as an instrument for coordination and price fixing.
- Pressure, coercion and retaliation aimed at ensuring price coordination are not acceptable under the Portuguese Competition Law.

18. The AdC also highlighted that temporary disruptions to supply chain or any form of public price announcement should not be used to hide or camouflage restrictive practices.

3. AdC's advocacy initiatives in times of food inflation

19. In the context of inflation, the AdC decided that it was key to reach out to stakeholders in Portugal, to raise awareness as to the role of competition in the context of inflation. As such, in August 2022, the AdC published an issues paper on “*Competition and purchasing power in times of inflation*”, with a set of key messages to the Government and to firms.⁸

20. In particular, the AdC highlighted mechanisms in which more competitive markets can play a key role in times of inflation. In addition, it was emphasized that each firm must set its own prices and strategies in the market in an autonomous manner (*vis-à-vis* their competitors in the market) and that temporary supply chain disruptions or any form of public price announcements should not be used to disguise a concerted practice.

21. The AdC has also made a few considerations regarding price controls as these are often implemented in times of inflation. In this context, it is important to draw attention to the potential risks to competition of imposing a price cap, as well as to likely alternative

⁷ Available here.

⁸ Available here.

policies that may achieve the same objective. The aim of the AdC in this regard is to contribute to informed policy decisions.

22. Indeed, during the inflationary context, many national governments have adopted measures to contain the surge in prices.

23. In Portugal, the government put in place several measures to support households in the face of the increase in prices, of which a temporary 0% VAT rate on a basket of essential food items. In addition to the VAT exemption, the government allocated €140 million in support to agricultural producers to help offset production costs and renewed extraordinary support program for agricultural diesel and fertilizers.

24. In this context, the government signed on 27.03.2023, a pact aimed at reaching a stabilization and reduction of food prices, with the Portuguese Association of Distribution Companies and the Confederation of Portuguese Farmers, to be in force for a period of 6 months and with a mid-term evaluation after 3 months. The VAT exemption was later extended for an additional period⁹.

25. This measure involved a Monitoring Commission, established to oversee the implementation of the measure, in which AdC was a member. Through its participation in the Monitoring Committee, the AdC took an observer role, ensuring only the necessary information was exchanged and that it did not result in a regime that could be used to distort or restrict competition.

4. Conclusion

26. Competition in the food supply chain is essential for maintaining lower prices, through downward pressure on profit margins and costs, to the benefit of consumer welfare and competitiveness of the economy. It is also key that firms take their market decisions autonomously and without sharing strategic and commercially sensitive information with their competitors.

27. From the point of view of vertical relationships in the food supply chain, retailers must determine their selling price unilaterally and without undue influence from upstream suppliers. These aspects are crucial to ensure competition in the market, to reduce the risk of supply disruptions and to offer better prices, more quantity and higher quality of the products to consumer.

28. As such, competition authorities must remain vigilant and make good use of their entire toolkit, advocating for pro-competitive policies, providing guidance and defending the market from any distortion or restriction of competition.

⁹ Bernardino et al. (2024). studied the effects of this measure using a high-frequency dataset of retail prices to assess the pass-through to consumer prices across different phases. They found that prices rose by about 1% after the announcement, but when the VAT cut was implemented, the pass-through to consumer prices was nearly complete (99% reduction in prices). Upon the reversal of the VAT cut, prices increased, but the pass-through was about 70%. Bernardino et al. (2024). “A Temporary VAT Cut in Three Acts: Announcement, Implementation, and Reversal”. Banco de Portugal, Economics and Research Department.