The Competition Authority
An tÚdarás Iomaíochta

Determination No. M/05/033 of the Competition Authority, 11 August 2005, under Section 21 of the Competition Act, 2002.

Notification No. M/05/033- H.J. Heinz Company/HP Foods Limited

Introduction

1. On the 22nd of June 2005 the Competition Authority, in accordance with Section 18 (1) of the Competition Act, 2002 ("the Act") was notified, on a mandatory basis, of a proposal whereby H.J. Heinz Company ("Heinz") would acquire HP Foods Limited ("HP").

2. On 12 July 2005, the Authority made a formal request for further information from both Heinz and HP, pursuant to Section 20(2) of the Act. Both Heinz and HP complied with the request by letters dated 15 July 2005, with attached documents. Hence 15 July 2005 is the "appropriate date" for the purpose of making and publishing of a determination, under Section 19(6) of the Act.

3. In the course of its investigation the Authority met with the Managing Director of Heinz Ireland, the parties' legal representatives and the retained economic experts. The Authority considered the parties' submissions and any evidence they provided. The Authority also considered evidence from the following sources:
    - Third party responses to telephone and written questionnaires – this included customers, distributors and competitors of the parties.
    - Internal business documents of Heinz and HP, provided in response to the Authority's request for further information.
    - Econometric analysis prepared by LECG ("LECG paper"), on behalf of Heinz and for the express purpose of the proposed acquisition.
    - Econometric analysis and economic advice provided by Dr. Vincent Hogan, University College Dublin, who was retained by the Authority.

The Parties

4. Heinz, the acquirer, manufactures and markets processed food products throughout the world. Heinz is listed on the New York Stock Exchange. Heinz's principal products include ketchup, condiments and sauces, frozen food, soups, beans and pasta meals, tuna and other seafood products, infant food and other processed food products.

5. Heinz's activities in Ireland primarily consist of sales, marketing and distribution of all Heinz, John West, Farley's and frozen brands in Ireland, and include:
    - Ketchup, Sauces and Condiments: Heinz imports these products into Ireland, primarily manufacturing ketchup, sauces and condiments in the Netherlands.
    - Frozen Foods: Heinz has a manufacturing facility located in Dundalk that produces Weight Watchers products from Heinz frozen ready meals. Apart from this facility, Heinz has no other food manufacturing facilities in

Ireland. Heinz also imports a range of frozen foods into Ireland from the UK.

- Soups, Beans and Pasta: Heinz imports dry and wet soups, canned beans and pasta products from the UK.
- Infant Foods: Heinz imports a range of infant foods, biscuits, cereals and juices from the UK and Italy.
- Seafood: Heinz imports a range of products, primarily tuna and salmon under the John West brand in Ireland.

6. HP, the target, manufactures and markets processed food products in the UK and the US, and exports processed food products to approximately 75 countries including Ireland. HP's principal products include ketchup, condiments and sauces, herbs, spices and seasonings, food oils and dry side dishes. HP's principal brands include HP, Lea & Perrins, Daddies, Rajah, Green Dragon and Lotus. In addition HP distributes Amoy products in Europe on behalf of Danone, which owns the Amoy brand.

7. HP's activities in Ireland include:

- Ketchup, Sauces and Condiments: HP markets a range of sauces, in the Worcestershire sauce, brown sauce, ethnic and soy-based sauce segments.
- Food Oils: HP distributes sesame and chilli oil under the Amoy brand in Ireland.
- Dry Side Dishes: HP distributes various noodles under the Amoy brand in Ireland.

HP's ketchups, sauces and condiments are currently distributed by Allegro Limited a distribution company. HP's Amoy brand products are currently distributed by Richmond Marketing

8. The parties' activities in Ireland overlap in relation to ketchup, sauces and condiments. In particular the parties overlap in the provision of ketchup, barbeque sauce and Worcestershire sauce.

Product Market

9. In *Comp/M.1990- Unilever/Bestfoods*, the European Commission (the "Commission") distinguished between two sectors of production and sale of food products, namely, the production and sale of food products to the retail sector and the production and sale of food products to the food service sector. The Commission stated that the food services sector consists of supply to out-of-home eating and institutional catering. The Commission stated that the food service distribution channels have important features which distinguish them from the retail channels and which thus give rise to separate markets. These distinctions include a service dimension, separate sales forces, different price structures, different pack sizes and different health and safety regimes.

10. The parties submit that this distinction between the retail sector and the food service sector applies in Ireland. The Authority concurs with the Commission and the parties that there are separate product markets for food retailing and food service. The remainder of the determination is focused on the retail sector.

11. In *Comp/M.1802- Unilever/Amora-Maille* the Commission considered that the sauces and condiments sector consisted of 11 separate product markets: (i) pepper, spices and herbs (ii) salt (iii) cooking aids or bouillon (comprises a range of cubes, granules and, more recently, concentrated liquid sauces used for making gravies and meat, chicken and vegetable and fish based stocks, and for flavouring during the course of cooking (iv) fruit and vegetable condiments (v) mustard (vi) mayonnaise (vii) ketchup (viii) other cold sauces (béarnaise, tartar and exotic sauces etc.) (ix) hot sauces (x) salad dressings and (xi) vinegar.

12. In *Unilever/Bestfoods* the Commission confirmed that *ketchup* and *other cold sauces* were separate product markets. The Commission stated the following in relation to *other cold sauces* in the *Unilever/Bestfoods* decision:

> Other cold sauces are used to add flavour to a prepared dish. They include mayonnaise-based sauces ("béarnaise", "tartare", "cocktail") and "exotic" or "ethnic" sauces with a non mayonnaise base (Tabasco, salsa, guacamole).[par. 27]

13. On the basis of the Commissions' analysis in *Unilever/Amora-Maille* and *Unilever/Bestfoods* the parties submit that the relevant product markets in relation to the proposed transaction are: (i) ketchup and (ii) other cold sauces. As the Commission did not specify what products were in the other cold sauces market the parties submitted a list of products grouped by segment that they believed were in the market, namely: (a) brown sauce; (b) barbeque sauce; (c) chilli and hot sauces; (d) soy sauce; (e) Worcestershire sauce; (f) other thick sauces; (g) pickles, relish and chutney and; (h) other condiments.

14. The Authority follows the Commission and treats ketchup as a distinct relevant market for the purposes of analysing the proposed transaction between Heinz and HP.

15. With regard to the other cold sauces market submitted by the parties, the Authority undertook analysis to clarify whether the barbeque sauce and Worcestershire sauce segments were each distinct relevant markets or part of a wider market such as other cold sauces. The evidence analysed in forming a judgement on the market for barbeque sauce and Worcestershire sauce included the parties' internal documents, econometric studies, customers' views and competitors' views.

Internal documents

16. The Authority agrees with the established principle that internal documents, prepared by undertakings in their ordinary course of business, provide a strong clear indication as to where an undertaking views itself in an industry, i.e. what its business is, who its customers are, and with whom it mainly competes. Similarly, the Commission has attached importance to internal business documents that may provide insight as to how parties view the market in which they compete.[1]

[1] See *Lagardère/Natexis/VUP* (Case COMP/M.2978, Commission decision of 7 January 2004) and *Coca-Cola Enterprises/Amalgamated Beverages GB* (Case COMP/M.794) and European Commission Market Definition Notice (OJ C 372 of 9 December 1997).

Barbeque

17. The parties' documents indicate that they perceive one another, Chef and Lakeshore as the main competitors in the barbeque sauce segment. However, more recent documents pay increased attention to the [number of other brands and innovativeness in the segment] as serious threats to sales. Accordingly Heinz launched 2 replacement recipes for its BBQ sauce *to* "[...]: "Classic" (based on hickory smoke) and "Hot" (based on jalapeno chilli)". The repositioning of Heinz's barbeque sauce reflects the innovative nature of the segment and the growing importance of chilli and hot sauces

18. A 2004 independent report by Mintel states that "Barbeque and other thick sauces such as chilli constitute a relatively new and buoyant market segment" and although "such products have been around for some years, the growing interest in barbequing has spawned an array of new barbeque sauces". The report also highlights the role Hellmann's Snack Sauce range and Heinz's Sauce Collection has had in driving growth in this segment of the market.

Worcestershire Sauce

19. Documents prepared on behalf of HP in relation to the sale of Worcestershire sauce in the State show that HP consider not only competitors who produce Worcestershire sauce (Heinz and Goodalls) but also competitors in the *"*Ingredients market*"* such as Sharwoods, Tabasco and Blue Dragon. Furthermore, a qualitative consumer study conducted by Research International on behalf of HP indicated that consumers use Worcestershire sauce as an add-on sauce (applied to prepared food) and as an add-in sauce (an ingredient in the preparation of a meal to enhance the flavour).

Econometric evidence

20. Both LECG and Dr. Vincent Hogan used product level data collected by AC Nielsen and provided by Heinz to conduct an econometric investigation of whether or not there was any evidence to support the hypothesis that BBQ and Worcestershire sauce are each distinct relevant markets. This provided sales volume and value for each of 560 products (differentiated by brand, serving size and container) in the ketchup, cold sauces and condiments sector[2] for each of the 26 months to May 2005.

21. The LECG paper investigates the degree of substitution between the different ketchups, cold sauces and condiments in the sample on the basis of an econometric model of demand. The LECG consultants undertook an econometric analysis to estimate elasticities from the demand system.[3] In a second step LECG perform a standard hypothetical monopoly test using

[2] The products were divided into 15 segments as defined by AC Nielsen: barbeque, brown, chilli and hot, soy, Worcester, other thick sauces, pickles, relish, chutney, other condiments, ketchup, mustard, mayonnaise, salad cream and salad dressings.

[3] LECG used the nested logit model of demand to estimate the elasticities. The nested logit model deals with cases where choices are made sequentially i.e. to purchase a sauce or not? Which segment of sauce to purchase from? Which brand of a particular sauce segment to purchase? See Berry, S., et al. (1995), "Automobile Prices in Market Equilibrium", *Econometrica*, vol.63, pp. 841-890, for an example where this approach is used to calculate mark-ups in the automobile market. Nevo, A. (2000), "Mergers with Differentiated Products:The Case of the Ready to eat Cereal Industry, *Rand Journal of Economics,* vol.31, pp.395-421 uses the method to evaluate the effects of a merger in breakfast cereal.

the derived elasticity estimates from the demand system. They investigate whether a hypothetical monopolist of each segment as defined by Nielsen would be able to profitability increase its prices by 5-10%. The LECG results indicate that barbeque sauce does not constitute a separate relevant market. In relation to Worcestershire sauce, they "believe the most appropriate of the results is that Worcestershire sauce is not a separate market."

22. The methodology in Dr. Hogan's study differs from the LECG methodology in that it imposes far fewer restrictions on the elasticities to be estimated[4]. Dr. Hogan uses the method of sequential demand system to estimate the elasticities[5]. This method ensures that the data is free to determine the elasticities. However, the cost for allowing flexibility in the model is that it reduces the statistical significance of the estimates. As a result a number of the elasticities were not statistically significant. However, of those elasticities that were significant the analysis suggested that Worcester sauce and chilli sauce were substitutes. The study also looks at the demand for individual products within segments to examine the degree to which other producers constrain the parties. For both the BBQ and Worcestershire sauce segments Heinz and HP are jointly constrained by other producers.

23. The proposed acquisition is analysed using two methodologies each of which has its limitations. The nested logit method used by LECG may be biased by imposing inappropriate restrictions on the elasticities. On the other hand, the model used by Dr. Hogan's suffers from low degrees of freedom. This renders most of the estimates statistically insignificant. Ultimately, both studies were consistent with the finding that neither Worcestershire sauce nor barbeque sauce are distinct relevant markets for the purpose of analysing the transaction.

Customer and competitor evidence

24. The parties' customers in the State are the multiples (Tesco, Dunnes Stores, Superquinn and Super Value), the symbol groups (Spar, Centra, Londis etc.) and the wholesalers. The multiples and the symbol groups have centralised purchasing managers who negotiate prices, discounts and special promotions with the parties. In general the purchasing managers believed that barbeque sauce was part of a broader market that included other thick sauces such as Hellmann's range of snack sauces and chilli sauces. As regards Worcestershire sauce, customers stated that the product was not similar to other cold sauces such as ketchup, barbeque or brown sauce but could be used as an add-on and add-in sauce.

25. None of the customers contacted raised objections to the proposed acquistion. The customers did not believe that as a result of the acquisition the Heinz/HP portfolio would enable the parties to implement a 5-10%

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[4] The LECG methodology forces cross price elasticities to be positive and that cross price elasticities are in proportion to market share. As these two restrictions are imposed, if they are not valid, the resulting estimates will be biased. Dr Hogan concludes in reviewing the LECG paper that "on balance the LECG approach may be a good approximation to reality".

[5] Hausman, J. and Leonard, G. (2000), "The Competitive Effects of New Product Introduction: A Case Study", *Journal of Industrial Economics*, applied this method to examine the US market for bathroom tissue and Rubinfeld, D. (2000), "Market definition with differentiated products: The Post/Nambisco Cereal Merger", *The Antitrust Law Journal,* vol. 68., pp. 163-185.

price increase to any of its products, including their barbeque and Worcestershire sauce offerings.

26. A range of ketchup, sauces and condiments producers were contacted. The general view of these producers was that the barbeque sauces faced competition from other thick sauces such as brown, chilli sauce and variants, spicy sauces and Hellmann's snack sauce range. None of the competitors contacted, including Chef the parties' biggest rival in the barbeque segment, had any concerns about the effects of the acquistion on the barbeque segment.

27. Chivers, a competitor of the parties that produces Goodalls Worcestershire sauce stated in their written response that Worcestershire sauce products faced competition from:

> Any flavour sauces. Any products [that] can be used as ingredients in cooking could be a directly or indirectly competitive product. For example, any sauces to give food spicy flavour, ginger flavour or any exotic flavours might be a competitor.

The respective distributors of Schwartz, Sharwoods, Oxo and Bisto all confirmed that their products which are used as ingredients in cooking would be indirect competitors of Worcestershire sauce. In fact, Schwartz's representative stated that some of their products contain Worcestershire sauce.

Conclusion on product market

28. The internal documents, econometric evidence and customer and competitor evidence indicate that neither barbeque sauce nor Worcestershire sauce should be treated as distinct relevant markets for the purposes of analysing the proposed acquisition. In particular barbeque sauce is a part of a wider market that at a minimum contains chilli sauces and other thick sauces such as Hellmann's snack sauces. The internal documents and the studies commissioned by HP relating to Worcestershire sauce clearly point to it being both an add-on sauce and an add-in sauce.

Competitive Analysis

29. The section considers the competitive effects of the acquisition in the retail market for ketchup, barbeque sauce and Worcestershire sauce. Each product is considered separately below. Both the barbeque sauce segment and the Worcestershire sauce segment are analysed firstly by looking at the competition within the segment itself and then by examining the competitive pressure exerted on the segment by those other products highlighted in the product market discussion as being competitors. The analysis shows that there will not be a substantial lessening of competition in any market for goods or services as a result of the acquisition by Heinz of HP.

Ketchup

30. As Table 1 illustrates Heinz is the market leader in ketchup with a share of [50-60]% of the market. Daddies, HP's ketchup brand, has a market share of [0-10]%. The acquisition will lead only to a minimal increase in Heinz's market share. There will remain an extremely strong competitor in Chef and the increasing prevalence of private label products is likely to continue as in other European countries. As such, the proposed acquisition will not give rise to a substantial lessening of competition in the market for ketchup in the State.

Table 1: Market shares in the ketchup market in the State, 2004

Ketchup Brand	Market Share by Value
Heinz	[50-60] %
Chef	[30-40] %
Private Label	[0-10] %
Kandee	[0-10] %
Daddies (HP)	[0-10] %
Others	[0-10] %

Source: AC Nielsen Market Track, provided to the Competition Authority by the parties.

Barbeque sauce

31. The barbeque sauce segment in Ireland has three large players (Chef, Heinz and HP) and a number of smaller players such as Lakeshore. Post-acquisition Heinz/HP would be the largest player in that segment accounting for approximately [40-50]% of the sales of barbeque sauce in the State. Chef would remain a strong competitive force accounting for approximately [20-30]% of the sales in the State. The econometric evidence highlighted that Heinz and HP are jointly constrained by third party products in the barbeque sauce segment.

32. The section on product market above highlighted that there has been a growth in barbeque brands and a movement towards chilli and other innovative flavoured sauces. Both Roma and Ainsley Harriot barbeque sauces have been launched in the last year and a half. The Ainsley Harriot brand now accounts for approximately [0-10]% of the sales of barbeque sauce in the State. The movement towards chilli is apparent in that the Ainsley Harriot barbeque sauce comes in two flavours: smokey barbeque and Mexican chilli barbeque.

33. The LECG econometric evidence suggests that a product in the barbeque sauce segment is constrained to varying degrees by all of the other 14 segments (e.g. ketchup, chilli etc…) examined in their study. LECG then investigated whether a hypothetical monopolist in the barbeque sauce segment would be able to profitability increase its prices by 5-10%. The conclusion was that a hypothetical monopolist in the barbeque sauce

segment would not be able to increase its prices by 5-10%. None of the estimates relating to the substitutability between the barbeque sauce segment and the other segments were statistically significant in Dr.Hogan's paper.

34. The customer and competitor evidence and the parties internal documents coupled with the econometric evidence indicate that the barbeque sauce segment is constrained at a minimum by the chilli and hot sauces and other thick sauces segments. These three segments together are three times the size of the barbeque segment in the State.

35. None of the parties customers contacted by the Authority had concerns with the proposed acquisition. The customers did not believe that as a result of the acquisition the Heinz/HP portfolio would enable the parties to implement a 5-10% price increase to any of its products, including their barbeque sauce products.

36. The acquisition will not enable Heinz/HP to profitably increase the price of any of its barbeque products by 5-10%. The Heinz and HP barbeque products are constrained by the other products in the barbeque segment and new entrants to the barbeque segment have been successful in taking sales from the parties. The parties are also constrained by those products in the chilli and hot sauce segment and the other thick sauce segment. Furthermore, the innovation which has characterised the evolution of those two segments is likely to continue and put increased pressure on "older" products such as barbeque sauce.

Worcestershire sauce

37. There are three brands of Worcestershire sauce sold in the State: Heinz, Lea & Perrins (HP) and Goodalls. Lea & Perrins account for approximately [70-80]% of sales of Worcestershire sauce in the State. Despite this the econometric evidence by both LECG and Dr. Hogan indicate that Heinz and HP are jointly constrained by Goodalls in the Worcestershire sauce segment.

38. The econometric evidence in Dr. Hogan's paper indicates that Worcestershire sauce and chilli and hot sauces are substitutes. This is consistent with the internal documents of HP which list Tabasco sauce as being a competitor. As already discussed, the internal documents of the parties clearly indicate that Worcestershire sauce is an add-in sauce as well as an add-on sauce. A study of the ingredients market in the State was carried out on behalf of HP by tns. The products listed in tns ingredients market exclude add-in seasonings such as those produced by Oxo, Bisto and Scwartz. These add-in seasonings are clearly marked in internal HP documents as being competitors, as such the ingredients market examined by tns does not take into account all the competitive constraints on the parties Worcestershire sauce products. Nonetheless, the study shows that the combined market share of Heinz and HP in the tns ingredients market is only approximately [0-10]%.

39. The acquisition will not enable Heinz/HP to profitably increase the price of any of its Worcestershire products by 5-10%. The parties ability to implement such a price rise profitability is constrained by Goodall's in the Worcestershire sauce segment, the chilli or hot sauces such as Tabasco and by the large number of alternatives in the add-in or ingredients

market such as the products of Sharwoods, Blue Dragon, Schwartz and Oxo.

Determination

The Competition Authority, in accordance with Section 21(2) of the Competition Act, 2002, has determined that, in its opinion, the result of the proposed acquisition by H.J Heinz Company of HP Foods Limited will not be to substantially lessen competition in markets for goods and services in the State and, accordingly, that the acquisition may be put into effect.

For the Competition Authority

Dr. Paul Gorecki
Member of the Competition Authority