The Tine Case - the question of dominance
ACE 2010

professor Tommy Staahl Gabrielsen,
University of Bergen

November 12. 2010

Disclaimer

The views expressed in this presentation are my own and not necessarily those of the Norwegian Competition Authority or the University of Bergen.

Outline

- A brief outline of the NCA's decision
- Tine - a cooperative
- The regulatory framework
- Cellophane Fallacy as a vehicle to establishing dominance

A brief outline of the decision

The Norwegian cheese market

- Extremely complicated market. Here are the main characteristics:
  - High import tariffs on cheese and milk. Norway has an exemption from the EEA-agreement.
  - Norway has high prices for cheese and poor product variety for cheese and other dairy products.
  - Norwegian government negotiates a total production quota for milk with farmers' associations
  - Tine - the main producer - is vertically integrated and a cooperative and has 70 - 90 % national market share for cheese.
  - Tine holds high prices in Norway, and exports excess milk through cheese and other products at low prices
  - Synnøve Finden - a cheese producer - is the only small national competitor.

The decision from NCA - dominance

- The dominance assessment in the decision from the NCA were based on the following elements:
  - the NCA made a qualitative assessment of properties with Norwegian cheese, and interviewed customers and consumers regarding substituability.
  - the NCA claimed that due to Norwegian regulations the prices of Norwegian cheese are already way above the competitive level, hence there is a Cellophane Fallacy problem.
    - The NCA claimed that as it can readily be decided that Norwegian prices on cheese are much more than 5 - 10 % above a competitive level, the question of dominance is settled.

- Prior to the decision Tine presented an empiricial critical loss analysis performed by Copenhagen Economics (CE).
- CE claimed that Norwegian cheese is part of a bigger market for sandwich spread that most likely are bigger than Norway
- In the decision the NCA had several objections to this analysis.
    - As prices already are increased significantly above the competitive level, a critical loss test based on such high prices will expand the market too much.
    - In spite of the fact the the test is performed on too high prices, the test could not delineate markets that are bigger than cheese.
- The NCA claimed that the analysis showed that Tine in fact holds a dominant position.

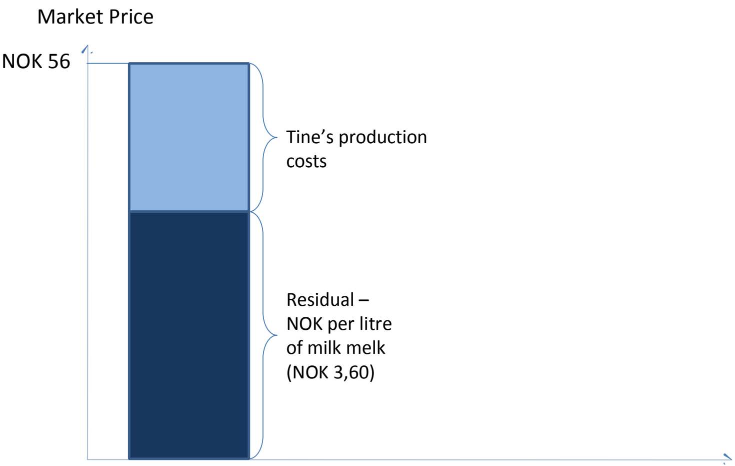
Tine - a cooperative

Tine - a cooperative

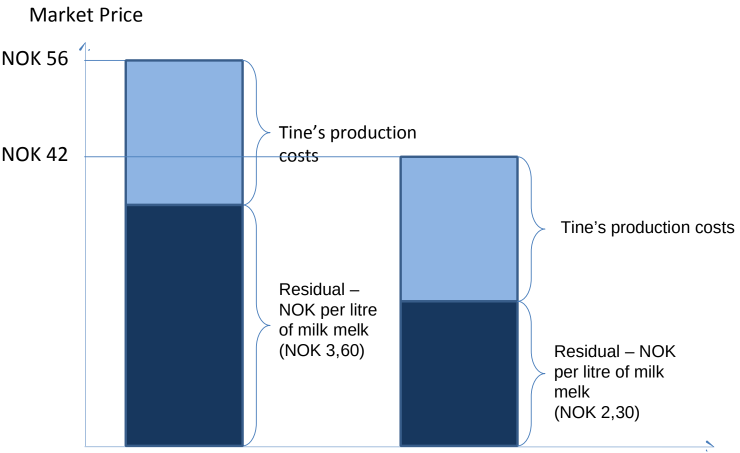
- Tine is owned by the milk farmers, and is vertically integrated into the dairy industry
  - Tine collects almost all milk in Norway
  - Tine sells milk to its downstream competitors, ie. a potential problem with margin squeeze
- Yearly negotiations between the Norwegian government and the farmers' associations determine
  - direct subsidies to the milk farmers
  - a total production quota for milk
  - a target price for milk, i.e., what Tine should seek to obtain for the milk
- Tine's main task is to ensure that the milk farmers get payed the target price for milk.

- This is done partly through that Tine produces dairy products and sells to the retailers, but Tine also exports dairy products and sells milk to its downstream competitors
- Taking the total revenues from Tines sale of milk and dairy products and subtracting Tine's costs yields a certain profit.
- Dividing this profit with the amount of milk in the system yields the milk price paid to the farmers
- This price shall ideally be equal to the target price set in the negotiations with the government
- Hence, the market for dairy products decides the milk price to the farmers as a residual when Tine's costs are subtracted from the revenues

An illustration



An illustration - reduction in the price of cheese



The regulatory framework

Regulations - some important issues

- Production quota for milk. Basically a milk cartel exempted from competition law.
- Import tariffs of approx. 50 % of the wholesale price of cheese to retailers.
- Prohibitive tariffs (at current prices) on milk.
- In the downstream dairy sector there is competition, although fairly limited.
- Norwegian prices on cheese are approx 100 % higher than those of similar cheeses in for example Denmark.
- The regulations are put in place to give Tine the possibility to exploit sufficient market power so as to realise the target price for milk.

The SSNIP-test as a road to dominance

- Using the SSNIP-test requires that current prices in the market is not to a significant degree influenced by market power.
- If so, there may be a cellophane fallacy problem.
- Therefore: If it can be established that Tines current prices deviates by more than 5 - 10 % above the competitive level, the question of dominance is settled.
- This question highlights the biggest disagreement between the NCA and Tine's experts.

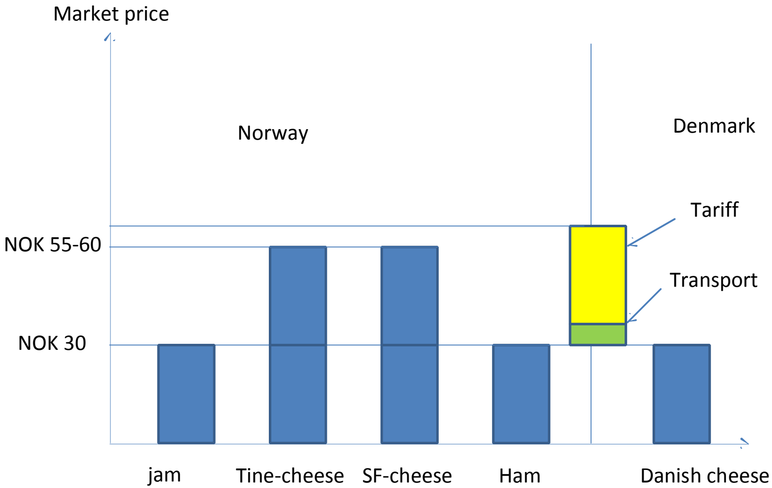
- O'Donoghue og Padilla:

"..estimating the competitive price level would transform the SSNIP test into a direct test of dominance. If, somehow, the competitive price level could be identified, then there would be no need to go through the whole process of defining the relevant markets and assessing dominance on the basis of structural and behavioural proxies."

- In general the challence is to identify the competitive price level.
- In this case, however, it is fairly easy to establish that the current prices charged by Tine is way (more than 5-10 %) above any reasonable estimate of a competitive level.

The competitive price level

- Two key observations:
  - Tariffs of 50 % of wholesale value to retailers
  - Danish prices are 50 % of Norwegian prices for comparable cheeses
- An illustration to show this


Market price
Norway
Denmark
Tariff
Transport
NOK 55-60
NOK 30
jam
Tine-cheese
SF-cheese
Ham
Danish cheese

Conclusions

- Tine has already exploited its market power due to Norwegian regulations and protection from international competition
- The SSNIP-test implied in this is a direct test of dominance, no further investigations is required
- The fact that Tine has no incentives to increase prices further has no relevance to the question of Tines dominance
- Having a dominant position is of course not unlawful, but it is unlawful for a firm to abuse its dominant position.