Insight

FTC Win in Grocery Case Has Long-term Implications

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Executive Summary

- On December 10, a Federal District Court for the District of Oregon granted the Federal Trade Commission (FTC) a preliminary injunction blocking Kroger's $24.6 billion acquisition of Albertsons, finding that the merger would substantially lessen competition among traditional supermarkets.
- The FTC's complaint relied on narrow market definitions and was a mix of long-established antitrust theories of consumer harm and more novel theories involving competition for unionized grocery labor that, in part, served as a test case for some of the changes made in the 2023 Merger Guidelines.
- While the specifics of the case are important to digest, the long-term effects on enforcement policy stem from the court's endorsement of lower market concentration thresholds and the consideration of labor markets in the 2023 Merger Guidelines.

Introduction

On December 10, a Federal District Court for the District of Oregon granted the Federal Trade Commission (FTC) a preliminary injunction blocking the $24.6 billion merger between supermarket chains Kroger and Albertsons. An hour after the ruling, a separate decision was handed down by a judge in Washington blocking the deal in that state.

The FTC's case relied on narrow market definitions and was a mix of long-established antitrust theories of consumer harm and more novel ideas involving competition for unionized grocery labor. As previously explained in a previous American Action Forum (AAF) insight, the FTC's case also served, in part, as a test for some of the changes made in the 2023 Merger Guidelines.

While the specifics of the case are important to review, the longer-term effects on enforcement policy stem from the court's endorsement of lower market concentration thresholds and the consideration of labor markets in the 2023 Merger Guidelines.

Details of the Ruling

Market Definition

The FTC contended that traditional supermarkets and supercenters – referred to as "supermarkets" – is the proper relevant market. This definition excluded other grocery retailers including club stores, limited assortment stores, dollar stores, and e-commerce retailers. The court agreed. The judge's opinion stated that "supermarkets are distinct from other grocery retailers. Supermarkets offer a larger selection of fresh and non-perishable items, a one-stop shopping experience that appeals to a particular customer's preference to meet all their grocery needs in one location, and a customer service focus with deli, bakery, meat, and other specialized departments." The court added that "the evidence that industry professionals understand supermarkets to be a distinct category of stores that compete with each other, and that supermarkets monitor each other's pricing and are sensitive to changes bolsters the conclusion that supermarkets are a submarket within grocery retailers." Moreover, the judge explained that "it is not surprising that consumers spend money at a variety of different types of retailers, but this does not necessarily show that those retailers are reasonably interchangeable substitutes for a consumer's particular needs," and that "a 'Costco run'" is not "a reasonable substitute for a weekly one-stop visit to a supermarket to purchase most or all grocery items for the week."

Past AAF insights have routinely commented on the tendency of the FTC and the Antitrust Division at the Department of Justice to leverage narrow market definitions to show a greater level of market concentration both pre- and post-merger. As became evident in the Kroger/Albertsons case, "restricting the relevant market to supermarkets represents a static view of competition for grocery sales that does not reflect a decades-long reconfiguration in market participants and ignores changes in consumer preferences that have broadened the scope of competitors." A more thorough accounting of the flaws in the FTC's case against Kroger and Albertsons can be found here.

Divestiture Plan

With the market definition limited to only traditional supermarkets, Kroger and Albertsons needed to convince the court that their divestiture plan would negate any anticompetitive effects of the merger

As part of the proposed merger, Kroger and Albertsons agreed to sell some stores to C&S

Wholesale Grocers. But this divestiture plan was met with immediate skepticism from the FTC, which argued in the original complaint that the proposed divestiture package "lacks the scale and necessary assets…that [Kroger and Albertsons] rely on today to successfully operate their respective businesses." Moreover, the agency added that C&S has "limited supermarket operating experience" and "is a poor choice for a divestiture buyer and increases the likelihood that the divested stores will flounder or fail."

The court agreed with the FTC. The court found that, even with the proposed divestitures, "many geographic markets will remain presumptively unlawful."

A Test of the 2023 Merger Guidelines

The court's decision, in part, included explicit endorsements of the 2023 Merger Guidelines that have implications for enforcement beyond this matter.

In the section of the ruling discussing competitive effects and measures of market concentration, the analysis conducted by Kroger and Albertsons relied on concentration thresholds found in the previous 2010 Horizontal Merger Guidelines. The expert in the case explained that he used the "2010 presumption thresholds because those in the 2023 Merger Guidelines are 'unreasonably low' and because the 2023 Merger Guidelines have not yet been adopted by any court." Yet the judge explained that "in the short time in which the 2023 Merger Guidelines have been in effect, multiple courts have cited them as persuasive authority without weighing their relative merits vis-à-vis the 2010 Merger Guidelines." Notably, the judge added that "the Court sees no reason to reject the 2023 Merger Guidelines in favor of a previous edition."

The judge's acceptance of these lower concentration thresholds has far-reaching implications for future antitrust litigation, as I previously discussed in comments submitted for the record on the 2023 draft Merger Guidelines. Primarily, the concentration ratios and changes in the concentration ratios establish a structural presumption rather than using concentration ratios as an initial screening mechanism. The authors of the 2010 Horizontal Merger Guidelines warned that "market shares may not fully reflect the competitive significance of firms in the market or the impact of the merger," and that they are to be "used in conjunction with other evidence of competitive effects." Further, more mergers will be considered illegal.

The judge's decision also endorsed the FTC's consideration of labor markets as a relevant antitrust market. The judge explained that "although the inclusion of workers in the 2023 Merger Guidelines is new, the concept of antitrust protections that extend to workers, not just consumers, is not." While the judge did not reach a conclusion with respect to the labor

market, the decision stated:

> *given that the FTC only recently included labor markets in the Merger Guidelines, the parties' arguments are understandably less developed than those regarding anticompetitive harm to consumers. There is no apparent exemption or prohibition against considering the labor theory and plaintiffs present a compelling and logical case for applying traditional antitrust analysis to labor markets. However, the limited evidence presented at this time is not sufficient to independently support a preliminary injunction.*

Yet the judge left the door open for the FTC to further develop its theory in this narrowly defined market, stating that "based on the limited evidence presented, the Court tentatively finds that the proposed union grocery labor market, including the [collective bargaining agreements] areas geographic market, is a plausible relevant market for antitrust purposes." An AAF insight has questioned the economic realities of such a narrowly defined labor market.

Until now, as the judge explained, the courts have cited the 2023 Merger Guidelines without "weighing their relative merits vis-à-vis the 2010 Merger Guidelines." This ruling changed that. The judge's ruling included direct endorsements of some of the most pointedly contested components of the 2023 Merger Guidelines, something the FTC's leadership needed for these guidelines to have their intended effect of reducing merger activity beyond the current makeup of enforcers.

Conclusion

The FTC prevailed in its effort to block the merger between supermarket chains Albertsons and Kroger as a district court agreed that the tie-up was likely to substantially lessen competition of traditional supermarkets.

While the merits of the case, including market definitions, are likely to be debated, it will likely have longer-term effects on enforcement policy. The FTC earned the court's endorsement of lower market concentration thresholds and the considerations for labor markets – and the narrow market definition used in this case – included in the 2023 Merger Guidelines.