Insight

Pepsi and Coke Targeted for Price Discrimination

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Executive Summary

- The Federal Trade Commission (FTC) launched a preliminary investigation into Coca-Cola and PepsiCo alleging that the beverage makers offered lower prices to larger retailers and are thus in violation of the Robinson-Patman Act (RPA), a law that prohibits price discrimination between large and small retailers for like products.
- President Biden's executive order on Promoting Competition in the American Economy inspired the revival of this long-dormant law as the FTC continues to advance its "return to fairness" doctrine and replace the nearly 50-year-old consumer welfare standard of enforcement.
- If the FTC is successful in its potential challenge, companies would likely respond by raising prices for large retailers, perhaps leading to a shift from savings for consumers to profit for suppliers.
- Using the RPA to protect small businesses would translate into higher prices for the end consumer, an easily avoidable outcome if the FTC had simply followed the consumer welfare standard.

Introduction

The Federal Trade Commission (FTC) reportedly launched a preliminary investigation into beverage manufacturers Coca-Cola and PepsiCo "over potential price discrimination in the soft drink market." The two soft drink makers allegedly offered lower prices to large retailers compared to their smaller clients. The FTC is gathering information from large retailers, including Walmart, requesting "data and other information on how they purchase and price soft drinks."

Underpinning the FTC's investigation is the Robinson-Patman Act (RPA). Passed in 1936, the RPA aims to protect competition by preventing price discrimination "between different purchasers of commodities of like grade and quality…." Only two cases have been brought under this often-forgotten law since 1998, however, as the RPA's relevance dissipated when agency enforcement shifted focus toward consumer welfare and away from a "big is bad" antitrust regime that protected smaller competitors.

It is likely that resurrecting the RPA would subject industries beyond beverage manufacturing to its provisions. Prohibiting producers from offering reduced prices to bulk purchasers to protect small businesses would translate into increased prices for the consumer at a time when inflation is near a four-decade high—and it would likely shift those consumer savings to profits for beverage manufacturers. Moreover, the action shows a disregard for nearly 50 years of antitrust enforcement guided by the consumer welfare standard.

Background and Revival of the Robinson-Patman Act

As previously explained by American Action Forum, Congress passed the RPA in 1936 in response to the growth of large grocery chains buying goods directly from suppliers and cutting out wholesalers. As a result,

smaller firms still reliant on wholesalers could not acquire goods at the same prices and were therefore unable to match the final sale prices offered by their larger competitors. The law was intended to protect these smaller, local stores from being priced out of the market.

President Biden's executive order (EO) on Promoting Competition in the American Economy that prompted the revival of this law. The EO directed the chair of the FTC "to improve farmers' and small food processors' access to retail markets" and investigate the "effect of retail concentration and retailers' practices on the conditions of competition in the food industries including any practices that may violate the Federal Trade Commission Act, the Robinson-Patman Act…or other relevant laws…."

Though the RPA has been dormant for over 20 years, FTC Commissioner Alvaro Bedoya recently called for the statute's enforcement as part of the agency's plan to "return to fairness." Bedoya's call for enforcement echoed a June 2022 FTC policy statement in which the agency announced its intention to leverage the RPA to target rebates and fees paid to pharmacy benefit managers.

Former FTC Chair and George Washington University antitrust Professor William Kovacic commented that, "At a symbolic level, restoring some level of Robinson-Patman Act enforcement delivers on the promise of the new leadership to give greater protection to small businesses."

Nevertheless, reviving the RPA will ultimately harm consumers in the form of higher prices at larger retail chains.

The Potential Case Against PepsiCo and Coca-Cola

In a potential case against PepsiCo and Coca-Cola, it is likely that the FTC will be able to show that the two beverage makers offered lower prices to larger retailers compared to smaller ones. A successful defense will rest on PepsiCo and Coca-Cola's ability to show that any price disparity between large and small retailers is directly attributable to a difference in the cost of supply. Alternatively, the beverage makers could show that any price concession given to the larger retailer was to meet a competitor's price.

Focusing on the first defense strategy, it is reasonable to suspect that PepsiCo and Coca-Cola face a lower per-unit cost of supplying a larger retailer relative to a smaller one. Coca-Cola and PepsiCo can leverage economies of scale in production and shipping in a way they cannot with a smaller supplier. Furthermore, it may not be economically feasible for PepsiCo and Coca-Cola to deal directly with small retailers, leaving the smaller firms to purchase from wholesalers.

Implications for the Consumer

Congress must be vigilant of the unintended consequences of the RPA. While successful enforcement will likely benefit small businesses, it would come at a cost to consumers in the form of higher prices.

Specific to the potential case against PepsiCo and Coca-Cola, if the FTC is successful at mandating price parity between small and large retailers, the most likely method of compliance by the two firms will be to raise the price of goods sold to large retailers. It is improbable that the beverage makers can lower the price charged to smaller retailers enough to reach parity with their larger counterparts and satisfy the FTC while maintaining an economically viable transaction. More broadly, this outcome is likely to be the model for future cases brought under the RPA involving different industries.

These higher prices will ultimately be passed onto the consumer shopping at large retail chains, such as Walmart. Around 140 million customers visit Walmart in person or online every week. Nearly 53 percent of Walmart shoppers earn less than $50,000 per year with just over 26 percent of its shoppers earning less than $25,000. Enforcing the RPA to protect small competitors will cause harm to this segment of the population very sensitive to price changes at a time of historically high inflation.

Conclusion

The RPA has been collecting dust for over two decades – as an empirical, evidenced-based method of enforcement applying decades of economic learning focused on consumer welfare was solidified. Yet some among FTC leadership are seeking to use this long-forgotten law as an instrument to revert to a “fairness” regime of antitrust enforcement. A successful revitalization of the RPA will leave consumers with higher prices, not just for soft drinks, but for any good or service targeted by the law and falls afoul of the consumer welfare standard.