Examining the Competitive Impact of the Proposed Kroger-Albertsons Transaction

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on behalf of the National Grocers Association

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Good afternoon, Chair Klobuchar, Ranking Member Lee and Members of the Senate Committee on the Judiciary Subcommittee on Competition Policy, Antitrust, and Consumer Rights. Thank you for holding this important hearing on Examining the Competitive Impact of the Proposed Kroger-Albertsons Transaction.

My name is Michael Needler, Jr. and I'm the President, CEO and Majority Shareholder of Fresh Encounter, Inc. I want to note that my professional career started on Capitol Hill when I interned for the late Congressman Michael G. Oxley, and then spent a second summer interning for the House Financial Services Committee. Both summers taught me how difficult your jobs are and I am grateful for each of you.

We operate 100 grocery stores in Ohio, Indiana, Kentucky, and Florida. I am a 3rd generation grocer. My grandfather started the grocery business in 1964 after he bought 5 stores in Northwest Ohio throughout several rural small towns. My mother and father acquired the business from him in 1995 and my sister and I acquired the company from my father a little over 10 years ago. Our company's mission is to "Delight our Customers, Nourish our Communities and Inspire Pride in our Team." We operate with a culture rooted in Positivity, Appreciation and Resilience.

It is an honor to appear before you today to provide the independent grocer perspective on competition in the grocery sector and the potential impact of the Kroger-Albertsons merger.

The view from where the independent grocer sits is this: competition in the grocery sector is suffering from increasing concentration and unchecked buyer power by dominant retail chains who force suppliers to discriminate against independent grocers. The result is a system that benefits a select few at the expense of everyone else, including consumers, workers, and independent retailers and producers. Consumers have a narrowing range of choices to shop for the goods and services they need; entrepreneurs and independent businesses struggle to start and sustain businesses; and producers such as farmers and ranchers are forced to accept unfavorable economic terms, conditions, and prices imposed by the largest members of a consolidated supply chain. Rural communities, which are heavily served by independent grocers, are hit particularly hard by the higher prices, reduced choices, and diminished competition.

Although these problems are not new, the grocery power buyers have taken advantage of the COVID-19 pandemic to further entrench their economic power at the expense of smaller

competitors and producers. Independent grocers like me struggled throughout the pandemic to stock must-have products—such as essentials like paper towels and toilet paper, cleaning supplies, and critical packaged foods like canned soup. Meanwhile, large national chains have exercised their buyer power to demand on-time, complete orders, and in some cases to secure excess supply.

As a result, many independent retailers are forced to compete in an unfair playing field. A major reason is the Federal Trade Commission's failure to enforce the Robinson-Patman Act, a law passed by Congress over 80 years ago to prohibit anticompetitive economic discrimination against independent businesses and allow the free market to work. If the Kroger-Albertsons merger goes forward, the grocery sector will have another massive player and the retail sector will become further consolidated. Enforcement of the Robinson-Patman Act will be even more critical to ensure a competitive grocery sector, especially in rural areas.

Taking a step back, please allow me to set the stage for what is at stake here. Grocery is an approximately trillion-dollar retail segment of the U.S. economy. There are about 38,000 supermarkets across the country, employing approximately 5 million Americans. Independent grocers and wholesalers generate approximately 33 percent of American grocery sales, or $253 billion in sales. The independent grocery sector generates 1.1 million jobs, $42 billion in wages, and $36 billion in taxes. According to the Food Industry Association, the supermarket industry as a whole invested over $24 billion due to COVID-19 to help keep our employees and customers safe.

The size of independent grocery stores serving America's communities varies widely. A store in an urban area like New York City may be 5,000 square feet, a store in small rural area of Colorado may be 20,000 square feet, while a grocery store in a Chicago suburb may be over 60,000 square feet. Independent grocers have diverse owners, diverse customers, and diverse locations.

If a small rural town or a high-density urban neighborhood has a grocery store, chances are it is an independent grocer. Independent grocers cater to the communities they serve and have positively differentiated their businesses through their offerings, service, quality, and freshness of products, and by being a local business with a heart for the communities they serve. Many independent grocers are family-owned or employee-owned businesses that have been in business for generations. In many markets, we provide an outlet for small and local producers who are overlooked by the big players.

Independent grocers are also strong competitors. In addition to price, independent grocers compete through food quality, variety, and availability; selection of healthy options; selection of locally produced foods; cleanliness; checkout speed; and availability of staff; as well as accessibility and convenience of location. To remain competitive and keep food prices as low as possible, independent grocers operate with a median net profit margin of about 0.7 percent, according to the 2020 Independent Grocers Financial Survey, ranking the grocery industry among the lowest in recorded net profitability.

My own stores serve a broad spectrum of markets, ranging from rural communities to inner-city neighborhoods. In many cases, our departure from the markets would deprive that community of access to healthy and affordable food, creating a food desert. We operate under several banners, because my growth strategy has been built around acquiring similarly challenged independent retailers who have run out of time, energy or in some cases run out of money. When I was named President of Fresh Encounter in 2010, I was 28 years old. We had about 30 stores and we were facing very difficult decisions. Frankly, our back was against the wall. Our margins continued to experience pressure and our sales volumes were under constant siege. In many cases, we would see retail prices at the competition that were well below our acquisition costs. I determined that there was only one way to survive, and that was to grow.

My thesis for growth was that it would give us the ability to buy better, spread our overhead over more stores and hopefully enable us to survive. I took a big risk, leveraged the company, and provided personal guarantees that we would be successful. We doubled our revenue with the acquisition of a struggling company operating in contiguous markets. Once we felt we had properly integrated with that company, we found ourselves again at the table working on saving a third company, and then again, a fourth company which was being sold in bankruptcy. With each transaction, our size, scale, and sophistication grew. In 2021 we acquired another 51 stores in the Tampa market under the Save A Lot banner. Our Save A Lot stores offer limited assortment grocery shopping in smaller footprints than our stores in Ohio, Indiana and Kentucky. That brings us to where we are today, 100 stores over four states, employing approximately 3,500 teammates.

In spite of our growth and supply chain enhancement, and efficiencies of scope and scale we are still a small player among giants. The retail grocery playing field is increasingly dominated by a handful of national and international chains. Last year, Food and Water Watch estimated that the top four supermarket and warehouse chains comprise roughly 69 percent of the overall market. The top player is Wal-Mart, which alone captures more than one out of every three dollars that Americans spend on groceries. Kroger currently comes in at second at 13.9 percent while Costco (12.2 percent) and Albertsons (8.1 percent) round out the top four. Although market share calculations differ depending on how broadly the market is defined, the reality is that a small handful of companies hold tremendous power over consumers and the producers and manufacturers who grow and sell the food Americans eat every day. A combined Kroger and Albertsons at nearly a quarter (22 percent) of the national market only increases the influence that a few retailers have over the marketplace.

Now, again, big isn't always bad. As I said earlier, growth to achieve scale and efficiencies was our strategy to compete and thrive. So, I am not categorically against transactions in the grocery sector. However, the Kroger-Albertsons merger is on a different order of magnitude, so it warrants strong antitrust scrutiny.

Let me be clear: we are agnostic on this transaction. But from my perspective, there are three key questions that the Federal Trade Commission and this Committee should ask in reviewing this merger:

1. **Will the transaction give the combined Kroger-Albertsons anticompetitive "buyer power?"**
2. **Will the Kroger-Albertsons merger leave our local communities better off or worse off?**
3. **Will proposed store divestitures remedy potential anticompetitive effects of the proposed merger?**

The first question is whether the transaction would give Kroger-Albertsons anticompetitive "buyer power."

What do I mean by that? Well, the dominant grocery retailers have become so massive that they account for a majority of U.S. retail grocery spend. This makes them essential gatekeepers for America's food suppliers. And it gives them the power to impose unfair and discriminatory conditions on independent competitors. When a grocery chain can, with a single email, grant or deny a food supplier's access to a significant percent of American households it has the power to dictate terms and conditions to suppliers. When a customer can threaten that much of your sales in one stroke, you have to listen.

They can get away with it because the dominant grocery retailers are not nearly as dependent on a particular supplier as the supplier is on the retailer. Think about it, even if a food supplier has a substantial number of products compared to the overall number of products for sale in any grocery store (in the tens of thousands), the total amount provided by a single manufacturer is only a fraction of a grocery retailer's sales. And a grocery power buyer often enjoys a choice between potential branded suppliers for a particular product in addition to selling its own, private-label versions of the same product. A dominant retailer has a substantial advantage over its suppliers in a negotiation because the risk for the retailer, if the supplier refuses its demands and no deal results, is substantially smaller than it is for the supplier. As a result, the power buyer can extract discriminatory terms—better prices, more favorable terms, and unfair allocations of products. And because Robinson-Patman has not been enforced, they often have to comply.

The massive grocery chains with buyer power force suppliers to discriminate against independent grocers on price, terms, and product availability. For years, I have seen the dominant grocery chains receive exclusive access to certain products and product packaging and charge retail prices far below the wholesale prices I can get from suppliers. A few examples:

- Price Discrimination—Price discrimination has taken many forms where we miss out on price promotions or packaging with a lower per unit cost. It also comes in the form of less favorable payment terms. For example, certain power buyers demand and receive "scan-based payment" terms for suppliers, meaning they only pay once a product has been scanned for final sale to a customer. Meanwhile, we pay for products upon receipt (or within a fixed period), shifting the risk that a product sits on the shelves to me. These terms provide significant advantages for dominant retailers, who in effect receive free credit on their purchases and can stock a greater diversity of products, without taking on any risk that the products will take time to sell, or will not sell at all.

- Package discrimination—Certain package sizes or promotional packaging is only offered to certain grocers, but not independents like myself. Some manufacturers have stopped supplying large package size version of products—that consumers associate with greater value—to independent grocers while providing them to big box retailers or club stores. In addition, dollar stores use its buyer power to demand "cheater size" products, which include smaller amounts in a package that can then be sold at a lower price. These "cheater size" products create a false impression among consumers that they are paying a lower price for the same product they see at independent grocers.

As I already mentioned, Kroger and Albertsons are already two of the largest grocers in the country. Combined I understand they would capture about 22 percent of grocery sales instead of 13.9 percent and 8.1 percent respectively. That's a very large increase in concentration, and the FTC and this Committee should determine whether that increase will give the merged firm buyer power. If the answer is "yes," then enforcement of the Robinson-Patman Act becomes an even greater imperative.

The second important question is whether the Kroger-Albertsons merger is going to leave our local communities better off or worse off. The answer will be "worse off" if the merger reduces competition in local markets, increases food supply chain concentration, and decreases supply diversity nationally and regionally.

In many markets where Kroger and Albertsons both operate the merger will directly increase concentration (whether that can be addressed is my third question below). However, leaving that aside for the moment, the merger will also reduce competition if it results in even more economic discrimination against independent competitors.

How could that happen? It's simple. Grocery chains with anticompetitive buyer power can demand treatment from suppliers that suppliers can't afford to give to everyone. Remember, many food and consumer good suppliers have thin margins, too. To afford the treatment that their dominant customers demand, they have to shift those costs to customers who don't have the power to make take-it-or-leave it offers to their suppliers. It's like pushing down on one side of a waterbed. Pressure on one side just shifts the water to the other side of the bed.

In September 2020 when I was struggling to get any supply for certain products on my shelves, Walmart sent a letter to suppliers demanding 98 percent on time, in full deliveries and threatened a penalty of 3 percent of the cost of goods sold on suppliers that failed to comply. So suppliers did what they had to do to keep their lights on, they kept Walmart happy and passed the bill on to the independent grocer and the American consumer. In the current cycle of food price inflation and ongoing supply chain disruptions, this problem has only worsened. Again, just like a waterbed, power buyers' squeeze on suppliers meant they had no choice but to limit product offerings and demand inflationary increases on their smaller customers. For us, inflation and supply chain challenges represent a threat to our business and our customers. For dominant chains, it represents an opportunity to gain even more market share.

I want to address a few of myths about buyer power and economic discrimination against independent grocers:

Myth number 1: The dominant chains get special treatment because they are more efficient. Not true. They buy by the truck load; I buy by the truckload. Achieving efficient scale was critical for my own business. And as I mentioned earlier, I determined that there was only one way to survive, and that was to grow. Like many independent grocers, we use two national wholesalers that together purchase approximately 30 billion of dollars of product from grocer suppliers every year. They aggregate the demand of thousands of independent grocery stores and handle logistics and distribution. For example, independent wholesalers operate highly efficient billion-dollar-plus warehouse facilities, just like the big chains. This allows independent grocers to achieve the same economies of scale that the dominant grocery firms boast about. Economic discrimination is about market power, not efficiency.

Myth number 2: The dominant chains get special treatment because they are just better at moving product. In fact, the opposite is true. The pandemic brought this dramatically to light. My own stores' growth dramatically outperformed my big box competitors' stores, including Walmart's, during COVID-19 on many products categories. I think a lot of consumers were looking to stay closer to home and appreciated our attention to customer service and efforts to keep them safe. And we have great prices and customer service every day, pandemic or no pandemic. Yet suppliers would not give us fair allocation of product. Isn't it a just little suspicious that suppliers were favoring the underperformers, who just happen to be the partners that they can't refuse?

Myth number 3: Economic discrimination is ok because the dominant chains will pass through the savings and at least their customers will get the lowest prices. Wrong again. The big grocery chains don't offer low prices out of the goodness of their hearts. They offer low prices for the same reason we do: to compete and win customers. When their independent competitors get driven out of business, or compete with higher costs, the big chains face weaker or no competition. What do they do? They just increase their margins and charge higher prices. Independent wholesalers have crunched the numbers and it verifies what common sense tells you: in markets where the big chains face no grocery competition, they charge higher prices to the consumer. All consumers lose from anticompetitive economic discrimination against independent grocers.

Now you will no doubt hear that curbing inflation is a reason why Kroger and Albertsons need to get together to become an even more powerful buyer than either is on its own. But again, that can only happen if it faces robust local competition—particularly from independent grocers who offer innovative and locally-tailored offerings that the big box chains don't provide. If economic discrimination continues to raise independent grocers' costs, at some point they can't hang on and they no longer act as a competitive check on the big chains.

Indeed, since March 2020 price discrimination has gotten even worse, which has exacerbated inflation. Suppliers eliminated promotional allowances to independent grocery stores on many products. In many cases, promotional spend has not come back or has come back at only reduced levels. As a result, independents weren't able to offer the in store promotional prices that our customers expect. Rural areas are disproportionately hit by discriminatory inflation because independents serve those communities. But that was only half of the problem. Although

suppliers ended promotional allowances to independents, they did not change their every-day-low-price programs with the dominant chains. While our wholesale prices went up, the big chains' wholesale prices stayed the same.

When independent stores close, they also leave behind gaping holes in local communities – called food deserts. But this does not impact all communities equally. Independents largely serve rural communities and inner cities. That means when independents can't compete, or compete with a higher cost base, consumers in places like small rural towns in the West, Midwest, and South will be disproportionately impacted. Those regions have some of the strongest traditions of service by independent, local grocery stores and chains today. But that's at risk without enforcement of the antitrust laws like the Robinson Patman Act, which will be even more critical if the Kroger-Albertsons transaction goes forward.

The other way local and regional areas could be worse off is if the merger results in increased concentration throughout the grocery supply chain. When the big grocery chains drive out independent competitors, it increases concentration in grocery retail markets. This increases the buyer power of the dominant grocery companies. But it drives greater consolidation upstream in the grocery supply chain as well. Power buyers' demands on suppliers for lower costs are forcing consolidation among food and consumer goods manufacturers. A 2021 investigation by the Guardian newspaper found that 79 percent of the groceries in a basket of 61 everyday types of food and drink are being sold by four companies or fewer.

In addition to reduced product choice and increased prices for independent grocers and their consumers, greater concentration can result in anticompetitively low prices paid to independent producers, such as ranchers and farmers. Because of their bargaining leverage, dominant retailers can and do aggressively drive down the prices they pay to farmers, ranchers, and other suppliers. The result is that dominant retailers are capturing a greater and greater share of each consumer dollar spent on food, while suppliers are forced to lower the prices they pay to farmers, and market participants throughout the supply chain have less money to invest in expanding their businesses. All of this has a devastating impact on rural communities.

We've all seen how important a diversified food ecosystem is, especially in the face of the pandemic. Allowing a few players to exert power will result in a less diverse food system. Again, rural communities have the most to lose because many local and regional producers—like the ones we have successfully partnered with at Fresh Encounter—are located there. Concentration also makes the food supply chain less resilient and more vulnerable to disruption and shortages. As concentration among suppliers has increased, grocery manufacturing has also been consolidated. As a result, a smaller number individual factories—built on a massive scale—have become critical lynchpins in the supply chain. Closures of just a handful of meatpacking plants led to food shortages, and outbreaks at other food processing and dairy facilities continue to threaten future shortages.

The third important question to ask is whether the merger and proposed divestitures that Kroger and Albertsons make would address these any of these issues.

As Kroger and Albertsons acknowledge, there are many communities across the country that both companies serve. As I understand it, the companies' proposal is to divest the stores into a vehicle called "SpinCo" that would operate between 100 and 375 stores. Although that sounds like a large number, it's really not when one considers the size of the combined company. The Federal Trade Commission needs to carefully investigate whether divestitures can remedy local, regional, and national competitive harms—including the creation of anticompetitive buyer power. This includes looking all the markets where there is an overlap and determining in what areas the stores need to be divested to address local effects. The FTC must conduct a market-by-market analysis down to the street-corner level to ensure that the combination doesn't harm consumers and leave communities vulnerable.

Once the Federal Trade Commission has identified the full set of local markets that require divestitures to preserve competition, it will need to very carefully vet the buyer or buyers of the assets to ensure that the divested stores are able to maintain local competition. As I well know, operating a grocery store chain of that size is incredibly challenging for the reasons I've talked about today, including economic discrimination imposed by power buyers. The combined Kroger-Albertsons would have nearly 5,000 stores—more than ten to fifty times larger than the SpinCo. I can tell you from personal experience the SpinCo won't have the kind of bargaining leverage with suppliers that the power buyers have.

Making these stores into a strong competitor isn't going to be a Wall Street lark. Who the owners of the SpinCo are will be very important to these stores' success or failure. They should have deep experience in the industry and be prepared to make further investments in these stores and the communities in which they operate. We believe that divested stores will be more likely to succeed in the hands of strategic buyers rather than under the consolidated ownership of SpinCo. Stores should be sold to existing grocery operators that know how to effectively compete as small or mid-sized chains.

The failure of the divestiture required by the Federal Trade Commission in the Safeway-Albertsons merger is a cautionary tale. The buyer of 146 of the 168 divested stores filed for bankruptcy shortly after it acquired the stores. Many of the stores were closed at least temporarily, and some were closed permanently. A number of the stores were reacquired by Albertsons after the bankruptcy. All of this was tremendously disruptive to consumers, workers, and the local communities served by these stores. And of course, the failure of the divestiture meant that the remedy for a potentially anticompetitive merger failed.

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I repeat that we are agnostic on this transaction. However, this Committee and the Federal Trade Commission need to review the Kroger-Albertsons merger carefully to determine if it will promote competition or harm it. The grocery industry doesn't need another power buyer that can impose discrimination on its competitors. But whether this merger proceeds or doesn't proceed there is tremendous need for more antitrust enforcement in the grocery sector, especially the Robinson-Patman Act.

The consumer benefits when there is competition. Healthy competition forces all of us to get better. We can all agree though that when the rules are fair, the best players will play, and compete. We can win in retail grocery by offering service, quality, technology solutions, great shopping experiences and many more delightful attributes. However, when the rules of the game are not enforced, and those with the largest budgets dictate the rules of supply, then the smaller players will not be provided a fair opportunity to compete on the highest consumer decision point – price. Unfortunately, this ultimately ends poorly for the consumer as the smaller firms exit. Without true price competition, consumers ultimately pay more at the grocery checkout.

The number of independent grocers in America is declining due to the relentless economic discrimination and concentration imposed by dominant grocery chains with buyer power. When independent grocers leave, small towns begin to fall apart, and our government spends billions trying to reverse the food deserts that form.

It's too late after the independent grocers leave. Prevention through antitrust enforcement is the only way to stop this erosion. The Federal Trade Commission and Department of Justice need to dust off tools like the Robinson-Patman Act to protect the free market, independent businesses, the food supply chain, and America's consumers. This Committee should also consider updating Robinson-Patman to address its enforcement challenges and to ensure the law reflects the modern economic realities of grocery retailing.

Thank you for taking time to hear from an entrepreneurial retailer today. There are many pressing issues in our Country, and I feel that having a healthy grocery sector is as important to our Country as most topics we face. I welcome any questions you might have.