STATEMENT OF

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BEFORE THE

SUBCOMMITTEE ON COMPETITION POLICY, ANTITRUST, AND CONSUMER RIGHTS
SENATE COMMITTEE ON THE JUDICIARY

ON

EXAMINING THE COMPETITIVE IMPACT OF THE PROPOSED KROGER-ALBERTSON TRANSACTION

NOVEMBER 29, 2022

Chairwoman Klobuchar, Ranking Member Lee, Subcommittee Members, thank you for the opportunity to appear before you today on behalf of Consumer Reports as you examine the impact of the proposed Kroger-Albertson merger on competition and consumers.

Consumer Reports was founded 85 years ago. As part of our mission to work for a marketplace that is fair and just for all, we have emphasized the fundamental importance of competition for ensuring a marketplace that works for consumers, by empowering them with the leverage of choice, the ability to go elsewhere for a better deal. That motivates businesses to be responsive to consumers' interests, with more affordability, better quality, and new innovative thinking, in response to consumers' wants and needs.

Kroger and Albertson (the '*Parties*') claim that this merger will be good for consumers. As we explain below, we do not find this claim to be credible.

The effects of increasing market concentration and consolidation in the sector

Before we critically review the claimed benefits of the proposed transaction, it is important to place the proposed transaction within the overall trend of increasing concentration in the sector.[1] The harmful impacts of this increasing consolidation were discussed in the Judiciary Committee's hearing on *Beefing up Competition: Examining America's Food Supply Chain*.[2]

As Consumers Reports testified in that hearing, many consumers, particularly in remote rural and marginalized urban areas, lack food options that are accessible and affordable – a problem aggravated by over-concentration in grocery retail that has created "food deserts".

In addition, more acute vulnerabilities in an over-concentrated food supply chain have recently come into stark relief. Examples include COVID outbreaks causing widespread meat-packing plant shutdowns with ripple effects up and down

[1] For example, recently Albertson and Safeway merged in 2015. Kroger acquired Harris Teeter in 2014 and Roundy's in 2015

[2] https://www.judiciary.senate.gov/meetings/beefing-up-competition-examining-americas-food-supply-chain

the supply chain;[3] a ransomware cyber-attack which forced Brazil-based JBS Foods, one of the four top beef packers, to shut down all its U.S. plants temporarily;[4] and the baby formula shortage earlier this year.[5] In these instances, the lack of alternatives available to absorb the shock exposed dangerous vulnerabilities created by over-reliance on just one or a very few suppliers of critical products and inputs.

We are concerned that the proposed merger between the two largest supermarket chains by further increasing concentration and incentivizing consolidation up and down the food supply chain will make a bad situation worse. For the marketplace to bring meaningful options to consumers, there need to be meaningful options at all parts of the input, production, distribution, and marketing chain, from farm to table. For the marketplace to work for consumers, it has to be working for businesses that seek to reach them. It has to be working for everyone.

Critical review of the claimed benefits of the proposed transaction

We now discuss the proposed transaction, and why we are skeptical that the benefits of the deal claimed by the Parties will be realized. Our preliminary analysis based on publicly available data and information suggests that:

1. The transaction will result in significant lessening of competition as Kroger and Albertson are the two biggest US supermarkets that compete directly with each other. The most likely outcome is increased prices, fewer choices for consumers, and reduced supermarket access for some consumers.

2. The claimed efficiencies are uncertain, and are not merger specific (i.e. the services and service improvements claimed to be made possible by the proposed transaction could be delivered without the transaction). Moreover, given the reduction in competition, merger specific efficiencies, if any, will not

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[3] Michael Corkery and David Yaffe-Bellany, The Food Chain's Weakest Link: Slaughterhouses, New York Times, April 18, 2020, https://www.nytimes.com/2020/04/18/business/coronavirus-meat-slaughterhouses.html

[4] Fabiana Batista et al, All of JBS's U.S. Beef Plants Were Forced Shut by Cyberattack, Bloomberg, June 1, 2021, https://www.bloomberg.com/news/articles/2021-05-31/meat-is-latest-cyber-victim-as-hackers-hit-top-supplier-jbs

[5] David Leonhardt, The Baby Formula Crisis, May 13, 2022, https://www.nytimes.com/2022/05/13/briefing/baby-formula-shortage-us-economy.html

necessarily be passed on to consumers or enhance Kroger's ability and incentive to compete in the market.

3. Given experience and learnings from previous divestitures of local stores the proposed store divestiture by the Parties is unlikely to effectively preserve competition in the relevant market.

We conclude that this merger between the two largest supermarket chains will significantly lessen competition and lead to higher prices, fewer choices, and worse access for consumers in some neighborhoods.

1. The transaction will result in significantly lessening of competition and the most likely outcomes are higher prices, fewer choices, and reduced access to supermarkets for some consumers

First, the proposed transaction will result in the merger of the 1st and 2nd biggest supermarkets or 2nd and 3rd biggest hyper-stores by revenue as shown in the Figures 1 and 2 below. Given the pernicious effects of the concentration in this sector discussed above, this further consolidation is unlikely to lead to better outcomes for consumers or suppliers.

Figure 1

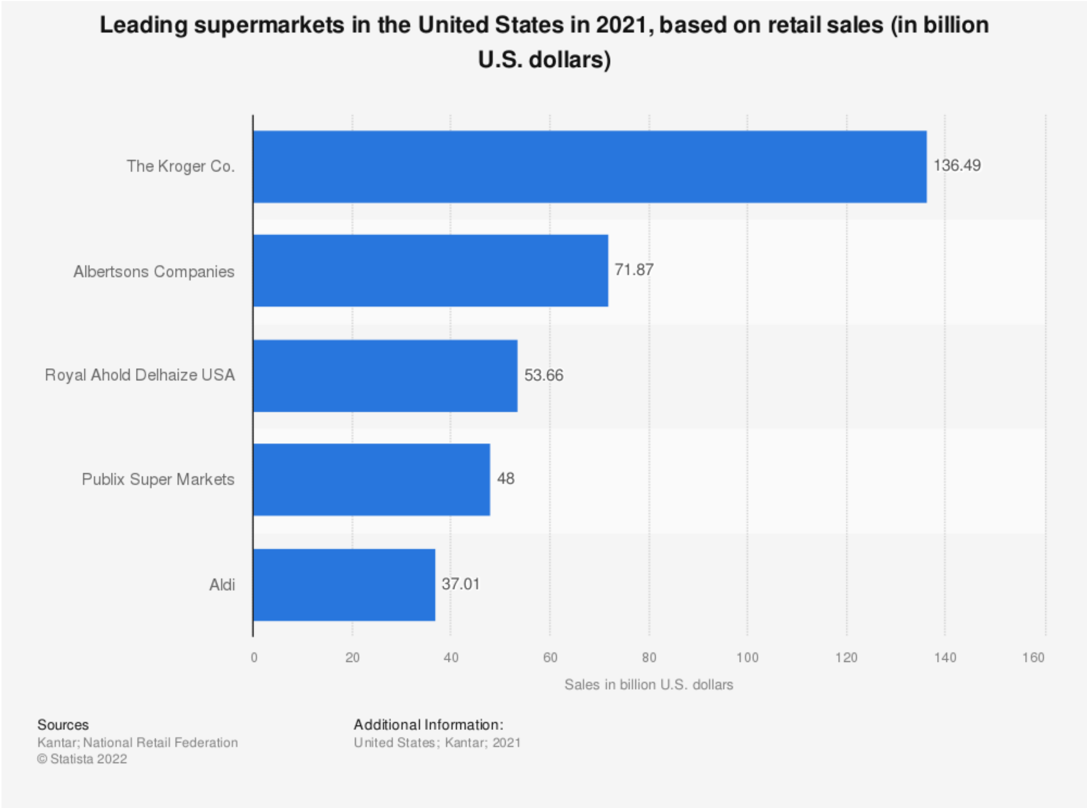
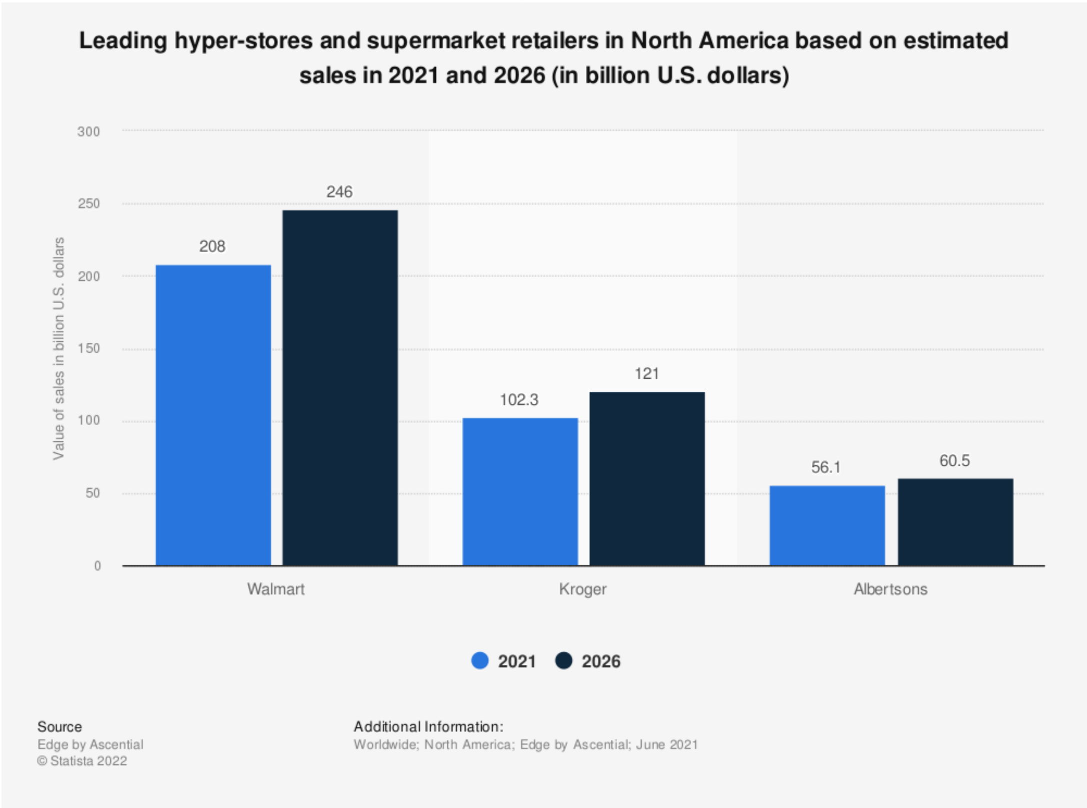


Figure 2



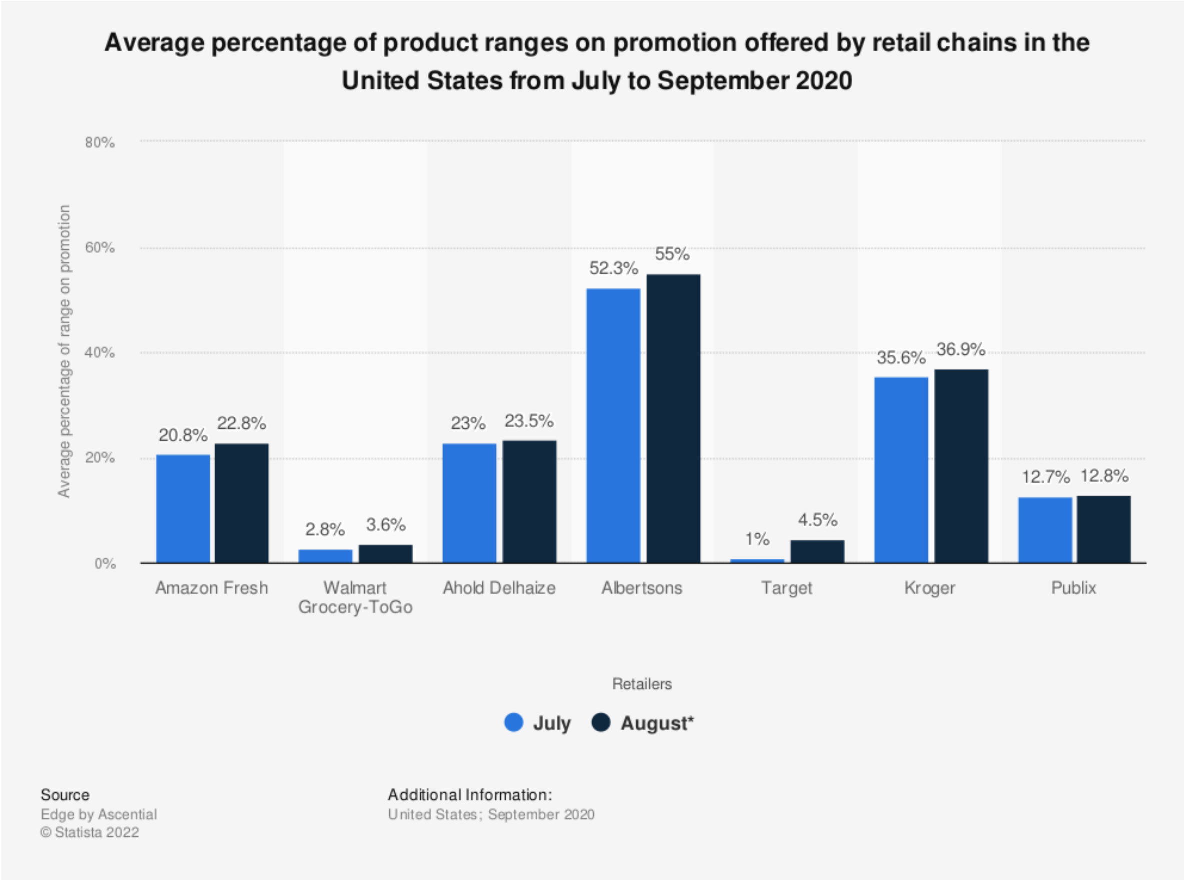
Second, Kroger and Albertson compete head-to-head in many markets. Kroger's 2021 Fact Book lists Albertson as one its main competitors in 5 out 10 of Kroger's top markets (major markets).[6] These 5 markets are – Los Angeles-Long Beach-Anaheim, CA (187 stores); Phoenix-Mesa-Scottsdale, AZ (98 stores); Dallas-Fort Worth-Arlington, TX (95 stores); Seattle-Tacoma-Bellevue, WA (84 stores); and Denver-Aurora-Lakewood, CO (82 stores) – a total of 546 Kroger stores. Out of a total of 49 major markers Albertson is listed as one of the main competitors in 14 markets covering 814 Kroger stores.[7]

One facet of this head-to-head competition between the independently owned and operated Kroger and Albertson is the number of product ranges on promotion or discounts to attract consumers. Compared to other retail chains both Kroger and Albertson have a much higher percentage of product ranges on promotion as shown in Figure 3 below. The proposed transaction if completed is likely to reduce incentives to offer these higher promotions as Kroger will no longer face competition from Albertson and vice versa.

[6] A major market is one in which Kroger operates nine or more stores. Kroger states it holds the #1 or #2 market share position in a majority of those major markets

[7] Appendix on Major Markets, Kroger 2021 Factbook, https://s1.q4cdn.com/137099145/files/doc_downloads/irw/fact_books/2022/2021-PDF-Fact-Book.pdf

Figure 3



Consistent with this expected effect, a 2012 FTC Bureau of Economics empirical paper, *Do Retail Mergers Affect Competition? Evidence from Grocery Retailing* finds support for the hypothesis that increases in market concentration resulting from mergers cause prices to increase when mergers take place in already concentrated markets. And this is a market that is already concentrated.

Moreover, these results are based on data from not just supermarkets but also club stores and supercenters. This is a wider market than that defined by the FTC in 2015 when it considered the Albertson Safeway merger. In that case the FTC found that *"The relevant line of commerce in which to analyze the Acquisition is the retail sale of food and other grocery products in supermarkets."*[8] Given the narrower market definition, it is entirely plausible that the price increase will be

[8] Para 9, FTC Albertson Safeway 2015 Complaint, https://www.ftc.gov/system/files/documents/cases/150127cereberuscmpt.pdf

higher when considering just supermarkets which are the predominant way that consumers shop for groceries and everyday essentials.[9]

The proposed consolidation of the Parties' store brand versions of food products and consumer goods will also reduce competition and choice for consumers. Kroger's Our Brands portfolio is currently the 9th largest U.S. CPG brands portfolio. The Parties' combined Our Brands portfolio will nearly double in size and become one of the largest CPGs in the U.S.[10] As Kroger states in its 2021 Factbook, Our Brands is an important competitive moat which Kroger has solidified over the years.[11] Kroger goes on to say that: "*The key to driving continued growth for Our Brands is our focus on innovation and new product development. We introduced 664 new Our Brands items throughout the year*."[12]

- First we note that the Parties' combined Our Brands Portfolio, one of the largest CPG's in the U.S., will further *deepen Kroger's competitive moat* i.e. enable it to keep competition at bay.
- Second, Kroger (and Albertson) innovation and new product development in Our Brands will likely slow down as the Parties focus on rationalizing their combined Our Brands Portfolio.

The most likely result: less competition and fewer choices for consumers.

Finally we note that consumers, especially in rural areas and high-density urban areas have poor access to supermarkets and grocery stores (as shown in Figure 4) and are often served by independent grocers.[13]

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[9] Some 72 percent of respondents answered the question "Where do you regularly buy food and products for everyday use?" with "Supermarket". Source: Statista Global Consumer Survey 2022

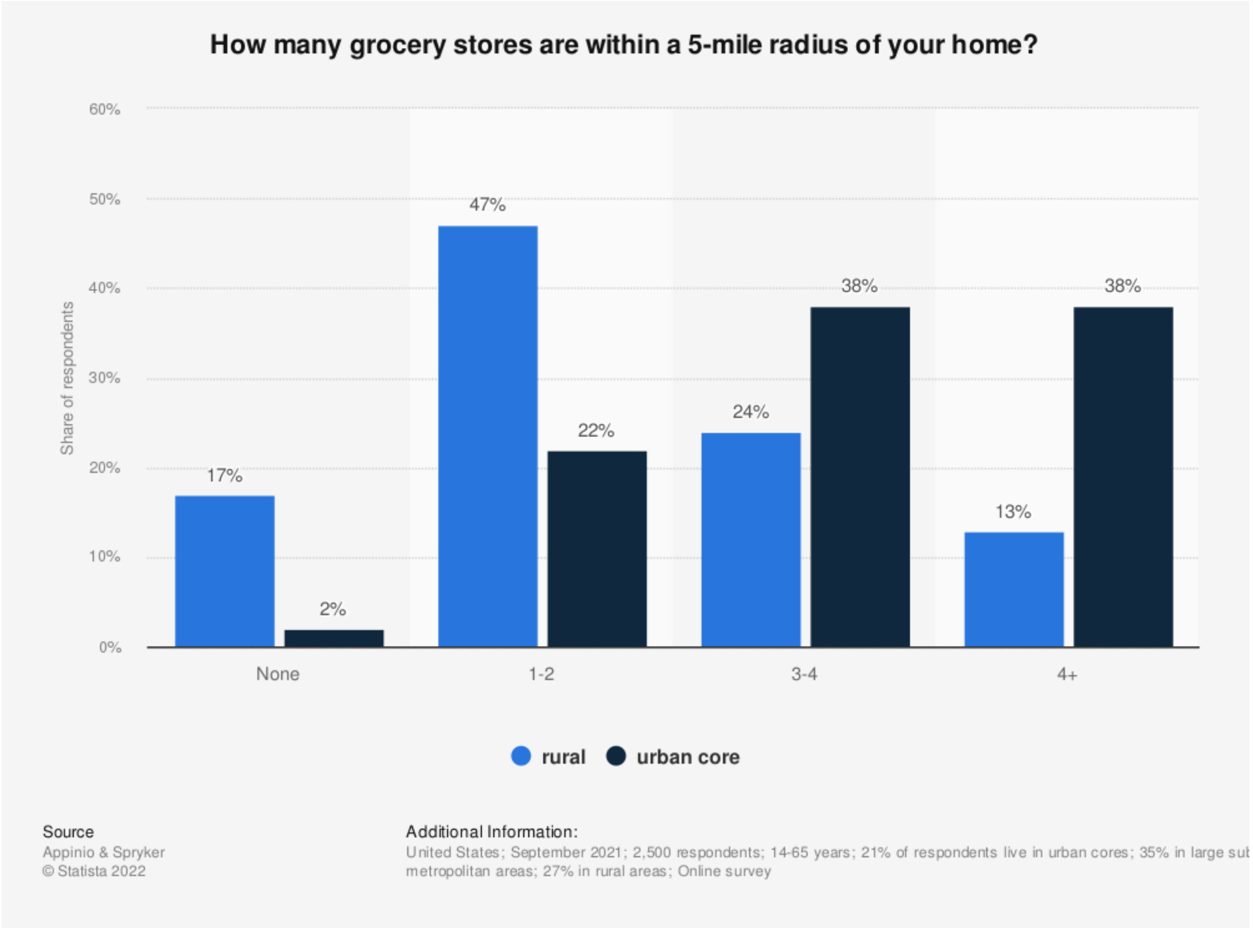
[10] Slide 16, Kroger-Albertsons Companies Merger Investor Presentation, 14 October, 2022, https://assets.website-files.com/6313a39c3c13ed1541dc24e1/63497445b7be8f45282920d4_Kroger-Albertsons-Companies-Merger-Investor-Presentation.pdf

[11] Page 8, Kroger 2021 Fact-Book, https://s1.q4cdn.com/137099145/files/doc_downloads/irw/fact_books/2022/2021-PDF-Fact-Book.pdf

[12] Page 17, Kroger 2021 Fact-Book

[13] See also the USDA's *Food Access Research Atlas*: https://www.ers.usda.gov/data-products/food-access-research-atlas/

Figure 4



The National Grocers Association has stated that dominant retailers can "*dictate terms and conditions to suppliers, including more favorable pricing and price terms, more favorable packaging, and access to exclusive products. Some even pressure suppliers not to sell certain products to independents.*"[14]

The proposed transaction will also increase the Parties' monopsony power i.e. market power on the buyer side and make it easier for Parties to impose favorable terms and conditions for themselves to the detriment of independent and smaller regional chains. The result will likely be even fewer choices for consumers in these areas. And a Consumer Reports survey in 2019 found that consumers overwhelmingly prefer their regional chains to national brands.[15]

[14] Testimony of Mr. David Smith, President And CEO, Associated Wholesalers Grocers, Kansas City, KS at the Judiciary Committee's hearing on Beefing up Competition: Examining America's Food Supply Chain
[15] Best Grocery Stores and Supermarkets, Consumer Reports, 16 April, 2019, https://www.consumerreports.org/grocery-stores-supermarkets/best-grocery-stores-and-supermarkets

2. The claimed efficiencies are uncertain, unlikely to be merger specific, and given the reduction in competition, merger specific efficiencies, if any, are unlikely to be passed on to consumers

The only efficiencies that are relevant in the context of a merger or acquisition are ones that can be shown to give the merged corporation clear ability and incentive to improve competition in the marketplace. This means that efficiencies must be actual and demonstrable, not vague, and speculative or aspirational. The Parties acknowledge the uncertain nature of any benefits of the proposed transaction in the Kroger-Albertsons Companies Merger Investor Presentation given:[16]

> "*… risks that the proposed transaction disrupts current plans and operations of Kroger and Albertsons; the ability to identify and recognize the anticipated benefits of the proposed transaction, including anticipated TSR, revenue and EBITDA expectations and synergies; the amount of the costs, fees, expenses and charges related to the proposed transaction; and the ability of Kroger and Albertsons to successfully integrate their businesses and related operations;…*"

This is understandable given the complexity of integrating and rationalizing different systems, store brand product portfolios etc. For example, Kroger has used Ocado for automated fulfillment and its own digital platforms to grow sales whereas Albertson's has used its omnichannel programs and partnered with Uber and Google to drive sales growth.[17]

The efficiencies also must be achievable only by merging – or what is referred to as "merger-specific." A short-cut to the corporation's desired growth is not an efficiency.

Kroger says in its Kroger-Albertsons Merger Investor Presentation that the deal "*Accelerates Kroger's go-to-market strategy*".[18] This may be good for Kroger

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[16] Safe Harbor statement, Kroger-Albertsons Companies Merger Investor Presentation, October 14 2022

[17] Errol Schweizer, Why A Kroger/Albertsons Merger Is A Bad Idea, Forbes, October 13, 2022, https://www.forbes.com/sites/errolschweizer/2022/10/13/why-a-krogeralbertsons-merger-is-a-bad-idea/

[18] Slide 4, Kroger-Albertsons Companies Merger Investor Presentation, October 14 2022

but it is not a merger specific efficiency that benefits consumers or gives Kroger a clear ability and incentive to improve competition in the marketplace.

For example, existing competition (pre-merger) incentivized Kroger to:

- launch Boost, it next generation loyalty program nationwide to deepen its relationships with its customers;[19]
- announce the opening of eleven central fulfillment centers and three additional regions (California, South Florida, and Northeast) as of March, 2022;[20] and
- open 17 new fuel locations in 2021.[21]

So the acquisition of more fulfillment centers or fuel locations is not a merger specific efficiency which gives Kroger the clear ability and incentive to improve competition in the marketplace as it seems to claim. It is investing in these facilities already.

A comparison of what Kroger claims it is already doing as presented in its 2021 Fact Book versus what it claims it could do after the proposed transaction as presented in its Kroger-Albertsons Companies Merger Investor Presentation is also instructive.

- The Go-to-Market Strategy on page 13 and the value creation model on page 43 of the Fact Book (pre-merger) are substantially similar to the claimed Go-to-Market Strategy on slide 9 and the value creation flywheel on slide 17 of Companies Merger Investor Presentation respectively. Note that both Kroger and Albertson currently offer similar services – stores, pharmacies, and fuel centers.[22]
- On slide 12 of the Companies Merger Investor Presentation Kroger seems to be claiming that it will be able to better personalize experiences and loyalty programs (post-merger). But on page 15 of its 2021 Fact Book Kroger claims it already has these capabilities (pre-merger). The difference seems to be that a combined Kroger Albertson will be able to analyze data from approx. 85 million

[19] Page 20, Kroger 2021 Fact-Book
[20] Page 21, Kroger 2021 Fact-Book
[21] Page 23, Kroger 2021 Fact-Book
[22] Slide 16, Kroger-Albertsons Merger Companies Merger Investor Presentation, October 14 2022

households post-merger rather than 60 million households pre-merger. No evidence is presented to suggest that the ability to analyze data on an additional 25 million households would materially improve capabilities to personalize experiences.

Finally, even if the Parties claim that there are some other efficiencies that are merger specific, these cost savings are unlikely to be passed on to consumers. Why would any of those savings be shared with consumers unless competition incentivizes the Parties to do so? These are after all profit-maximizing corporations.

For example, Kroger claims on slide 5 of its Companies Merger Investor Presentation that it will invest a billion dollars to continue raising associate wages and comprehensive benefits. It may do so, but these investments, as it explains in its 2021 Fact Book, are:[23]

> *"... driven by our data analytics research for specific areas to ensure our wages are competitive with the market. We will continue our efforts to rebalance pay and benefits, while also focusing on operational flexibility for our stores."*

This suggests that in specific areas where there are fewer stores after the proposed transaction, wages are likely to decrease as there will be fewer retail employment opportunities and Kroger will face less competition to hire workers for its stores.

3. The proposed divestiture of some local stores will not effectively preserve competition in the relevant market

The details of any divestiture being proposed by the Parties are unknown – for example the number of stores, whether these will be in proximity so they can form a regional network of stores, or whether the divested stores will have all business elements to operate independently.

But the logic of any divestiture in this instance is strange. The deal rationale given by the Parties (disputed as discussed above) is that it will allow them to be more competitive in the market by growing their store footprint, increasing the

[23] Page 37, Kroger 2021 Fact-Book

number of fulfillment centers, growing their store brand portfolio, and the ability to analyze data on more households. Yet the proposed Spin Co to be formed from the divested stores will have less of each of these assets. How is the Spin Co expected to compete *if* the deal rationale is to be believed? As the 2011 DOJ remedies guidelines explain:[24]

> "*The touchstone principle for the Division in analyzing remedies is that a successful merger remedy must effectively preserve competition in the relevant market. That is the appropriate goal of merger enforcement.*"

It is unclear how the divestment of a subset of Parties' stores will achieve this aim. Merging parties in general will have incentives to make sure that the purchaser of divested assets is not an effective competitor or at least not as effective a competitor as any one of the merging parties. This is illustrated by the failed divestment of 168 stores that the FTC required when Albertson and Safeway merged.[25]

Finally, we note that recent research suggests that when competition is national and supermarkets set prices nationally, local divestitures will not restore competition but may be counterproductive, and more so if the chains also compete locally along non-price dimensions such as quality.[26]

Conclusion

For all the reasons discussed above we remain skeptical that a proposed divestiture of a subset of the Parties' stores would effectively cure the loss of competition or enhance consumer welfare.

And based on our preliminary analysis set out above, we are skeptical that the benefits of the deal claimed by the Parties will be realized. The most likely outcome of this merger between the two largest supermarket chains will be to

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[24] U.S. Department of Justice, Antitrust Division Policy Guide to Merger Remedies, June 2011, http://www.justice.gov/atr/public/guidelines/272350.pdf

[25] Brent Kendall, Haggen Struggles After Trying to Digest Albertsons Stores, Wall Street Journal, , 9 October, 2015 http://www.wsj.com/articles/haggen-struggles-after-trying-to-digest-albertsons-stores-1444410394

[26] T Gabrielsen, , B Johansen, O Straume, Merger control in retail markets with national pricing, Working Paper in Economics, No. 10/22, Department of Economics, University of Bergen

significantly lessen competition and lead to higher prices, fewer choices, and worse supermarket and grocery access for consumers in some neighborhoods.

Thank you again for the opportunity to testify before you today. I am happy to answer any questions.