

**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE**

ROUNDTABLE ON COMPETITION ISSUES IN FOOD CHAIN INDUSTRY

-- Note by Turkey --

This note is submitted by Turkey to the Competition Committee FOR DISCUSSION under Item XII at its forthcoming meeting to be held on 30-31 October 2013.

JT03345963

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1. Introduction

1. Food retailing sector serves a critical function in connecting producers with final consumers, and it plays a key role in the formation of prices at all levels of the food supply chain. This note aims to briefly explain the transformation of food supply chain and the legal framework for food retailing in Turkey. It also attempts to address buyer power related competition problems based on the findings of the recent FMCG retailing market investigation finalized and published by Turkish Competition Authority (the TCA) in 2012.

2. Transformation of Food Supply Chain in Turkey

2. The food retailing sector has gone through a transformation period from small retailers to large nationwide (sometimes international) chains due to rapidly changing supply and demand conditions. The transformation of the food retail sector implies a process, which has resulted in organized retailers gaining power before both producers and conventional retailers, thereby triggering a transformation in the whole supply chain. This process, which changed the balance of power in the supply chain to the advantage of organized retailers may lead to some conflicts and tensions among various actors of the supply chain.

3. Since the beginning of the 1990s, the share of organized retailers in food retailing has been increasing in Turkey. Food retail constitutes the largest share in the total retail market with a turnover of US \$96 billion in 2010. The share of organized retailers in FMCG retailing grew from around 30% in 2005 to 50% in 2011. Although this implies an important growth rate for organized retailing, conventional retailing (small local shops, specialized shops, open bazaars etc.) still has an important role in food supply chain in Turkey.

4. In line with the growing pace of the organized retailers, as organized retailers growth gathered pace, many globally operating food retailers has decided to enter the Turkish market. International retail chains such as *Carrefour*, *Tesco* and *Metro/Real* operates in Turkey directly or through partnerships. Concentration levels have increased mainly due to acquisitions of smaller chains by the larger ones. Yet, concentration levels are still low compared to most of the European countries.

| Concentration Ratios in Organized Retailing | | | | | | |
|---|-------|-------|-------|-------|-------|--------------------|
| | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 (6 months) |
| CR3 | 20,57 | 20,23 | 21,56 | 23,03 | 23,38 | 23,36 |
| CR4 | 22,15 | 22,22 | 23,75 | 25,20 | 25,76 | 27,01 |
| CR5 | 23,44 | 23,66 | 25,13 | 26,61 | 26,96 | 28,41 |
| CR8 | 24,97 | 25,48 | 27,25 | 29,04 | 29,79 | 31,47 |

5. Organized retailing has been more developed in some regions of the country depending on the urbanization rate, the share of regions/provinces in the national income, consumer habits and differences in

the economic and social life and the mobility of consumers. These differences eventually generate different competitive conditions in food retailing in various regions.

6. Regional/local retailers, mainly operating in the supermarket channel, create important competitive pressure on national retailers in Turkey. In the last two years, regional/local retailers have grown by about 50% in terms of number of stores and total sales area and some local retailers formed joint ventures to create economies of scale in buying.

7. In the last decade the most remarkable change in the food retailing in Turkey is the rise of discount stores. Discount stores channel, has been the fastest growing channel during the 2004-2009 period, with about three-fold increase in turnover. Between 2004 and 2009 organized retailing grew by 94% in sales, while discount retailing grew by 182% in the same period. The high demand for discount stores may be seen as a reflection of increased price sensitivity of consumers. In Turkey, *BİM* is the leading discount store by a wide margin. In 2011 *BİM* became the retailer with the highest yearly turnover. *A-101*, which entered the market in 2008, also showed significant growth in a short period.

8. Private label product consumption has been increasing from 2006 to 2011. This trend is parallel to the increase in demand for discount stores. About 60% of the leading discount stores turnover comes from private label sales. Not only have discount stores sold private label. Other retailers have been increasing the amount of private label products in their product mix as well. In 2011 11% of turnover in the sector was generated by private label sales.

3. Legal Framework in Food Retailing

9. There has been legislation preparation for FMCG retailing for a long time. The first draft law on the FMCG retailing was submitted to the Parliament in 1999. Following that, many draft laws were prepared at various times with different scopes.

10. There are basically two motives behind the preparation of the relevant draft laws. The first is to protect smaller food retailers in the conventional channel from the competitive pressures by organized retailers. The second motive is to protect small- and medium-scale suppliers from the unfair practices of large chains following the growth in organized retailing and, in particular, difficulty faced by these suppliers in accessing the shelves of retailers. For the purposes of protecting the suppliers, the envisaged policy/method is to introduce limitations on fees demanded by retailers as well as on private label products and to prevent late payments. For the purposes of protecting conventional retailers, on the other hand, introducing authorization criteria concerning shopping centers and retail chains as well as limits for business hours is envisioned. The TCA has officially submitted its opinion on the aforementioned draft law to the relevant Ministry. The opinion emphasized that the draft bill generates asymmetrical regulation and creates entry barriers. The Ministry of Customs and Trade is working on a new draft and the TCA has been in touch with the Ministry during this period to remark competitive concerns related to the legislation.

11. On the other hand, the Turkish Commercial Law no. 6102 (TCL), adopted by the Parliament on 13.1.2011, introduced a limitation of sixty days for payment periods in commercial relationships in order to protect creditors (TCL, Article 1530). This provision is primarily introduced in order to protect the supplier in supplier-retailer relationships and it is compliant with the new directive of the EU, adopted at the end of 2010 to struggle with the problem of late payments. This new provision in the TCL seems to have eliminated one of the motives behind the preparation of the retail draft law.

12. There is no price regulation in food supply chain. In some sectors like tea and sugar, the production is still at the hand of state owned companies however those state owned companies do not act as price regulators. In some limited circumstances, the government might take some measures to effect

product prices as it happened in meat sector. In order to limit the dramatic increase in meat prices in 2010, the tax on livestock imports were decreased by the government for a certain time period.

4. Buyer Power Related Competition Problems in Food Retailing

13. The relationship between suppliers and retailers has changed in line with the increasing concentration in food retailing raising buyer power of retailers. Buyer power is related to how buyers affect trade conditions with sellers in the upstream markets. The fact that retailers possess buyer power means that they have a strong ability to affect trade conditions in their relations with the suppliers in their own interest.

14. On the one hand, the buyer power may generate some efficiencies, on the other hand it can also distort competition. Buyer power may balance market power of suppliers and this in turn may increase consumer welfare. Such a result necessitates a competitive retail market structure. If the powerful buyers feel competitive pressure from other retailers in the market, they would pass on the benefits they acquired from suppliers to consumers as decreased prices or better products.¹ Exercise of buying power might not benefit consumers if the buyer is not constrained by competitors and might distort competition in the downstream supplier markets. Large retailers might acquire advantageous terms of trade from suppliers due to buying in large amounts. This type of price reduction might not create competitive concern, however the discounts which are not related to cost efficiencies and which are just based on the use of buyer power might be detrimental to competition.

15. The TCA has received complaints from several suppliers about retailers' buyer power and related conduct. Problems between suppliers and retailers have also been addressed in the media. During the TCA's market investigation, interviews were made with both suppliers and retailers and a questionnaire was conducted for the both parties. According to the TCA's findings there are four main problematic areas within the commercial relationship between retailers and their suppliers:

- i. the unilateral imposition of contract terms (i.e. negotiations within a pre-set purchasing agreement);
- ii. discounts and related mechanisms;
- iii. penalties;
- iv. payment terms.

16. Large retailers demand additional fees, discounts and services from suppliers under various names such as listing fees, shelf space fees, display area fees (such as gondolas, pallets, shelf position, placement in accordance with the traffic within the store, etc.), insert fees, electricity fees, personnel requests, free products, store opening fees, anniversary fees, end-of-year discounts and that such practices are gradually spreading within the sector. Suppliers state that a significant difference appears between the gross prices and net prices of their products due to these fees and additional services, and that the suppliers' business is impeded since it is impossible to reflect these extra costs to the price due to competition.

17. To analyze supplier-retailer relations, the terms of transactions and the extent of problems supplier questionnaire applied to more than 500 suppliers and 209 of them fully answered the

¹ DOBSON P., WATERSON M. and CHU A. 1998, "The welfare consequences of the exercise of buyer power", Office of Fair Trading Research Paper 16, p.6.

questionnaire. Results show that the share of nationwide retailers in suppliers business is increasing gradually and has the highest share compared to other retail formats, on the other hand the share of traditional retailers and wholesalers in suppliers business is decreasing. The first four retailers share in supplier's business is increasing. In 2009 the share of first four retailer in supplier's business is more than 25%.

18. Agreements between suppliers and retailers are mostly written. Written agreements create transparency in transactions, and provide a ground for sharing the risks of the commercial activity between the parties in a foreseeable way. Questionnaire results show that agreement terms are changed rarely by the retailer and mostly determined by negotiation. 61% of the suppliers are not satisfied with the agreement terms. However dissatisfaction is for all the retailer formats, not just for the large retailers. In case of conflict between retailer and supplier, instead of going to court, solving the problem by negotiation is preferred.

19. 51% of suppliers expressed that the gross profit margin has been decreasing in the past three years. However, 92% of the suppliers answered that they don't have the concern of exiting the market due to the decrease in gross profit margin. Also delisting of their products is not seen as a big concern, the first reason for delisting a product is that it does not create the expected profit. 55% of the suppliers said they produce private label products for retailers, but they are not concerned that private label products are going to take place of their branded products.

20. Market investigation shows that buyer power of FMCG retailers is increasing, and as the sector keeps its growth rate, the buyer power of large retailers is expected to increase accordingly. However the problems expressed by most suppliers are similar for all retailers. Buyer power of large retailers is not distinct from other retailers. There is a general dissatisfaction about relations with retailers but the dissatisfaction is not directed to large nationwide retailers. Especially suppliers who produce in product categories with low level of brand and customer loyalty (like dairy, meat, legumes etc.) have less bargaining power and they live more problems in terms of contract terms. The most important finding is that suppliers are not economically dependent on any type of retailers and for now buyer power of large retailers is not at a level that would distort competition in the long run. Eventually, the TCA concluded that food retailing sector in Turkey is in an early stage in terms of concentration levels and buyer power when compared to most of the European markets, and therefore for the time being there is no need to take any measure against the matter of buyer power.