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Food-Retail Competition, Antitrust Law, and the Kroger/Albertsons Merger

Brian C. Albrecht
Dirk Auer
Eric Fruits
Geoffrey A. Manne

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laweconcenter.org | icle@laweconcenter.org
1104 NW 15th Ave. Ste 300 Portland, OR 97209

@laweconcenter
503.770.0076

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Brian C. Albrecht, Dirk Auer, Eric Fruits, & Geoffrey A. Manne[*]

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[*] Brian C. Albrecht is the chief economist of the International Center for Law & Economics (ICLE). Dirk Auer is ICLE's director of competition policy. Eric Fruits is an ICLE senior scholar. Geoffrey A. Manne is ICLE's president and founder. ICLE has received financial support from numerous companies and individuals, including firms with interests both supportive of and in opposition to the ideas expressed in this and other ICLE-supported works. Unless otherwise noted, all ICLE support is in the form of unrestricted, general support. The ideas expressed here are the authors' own and do not necessarily reflect the views of ICLE's advisors, affiliates, or supporters.

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Executive Summary

In October 2022, the Kroger Co. and Albertsons Cos. Inc. announced their intent to merge in a deal valued at $24.6 billion.[1] Given the Federal Trade Commission's (FTC) increasingly aggressive enforcement stance against mergers and acquisitions, as well as Chair Lina Khan's previous writings on food retail specifically,[2] the agency appears poised to try to block the transaction—even with divestitures.[3] The FTC and U.S. Justice Department's (DOJ) recently unveiled draft revisions to the agencies' merger guidelines further suggest that they plan to challenge more mergers—and to do so more aggressively than under past administrations.[4]

But attempting to block this transaction would go against the analytical framework the FTC has historically used to evaluate similar transactions, as well as the agency's historical precedent of accepting divestures as a remedy to address localized problems where they arise. Such breaks with the past sometimes happen; our understanding of the law and economics evolves. But in the case at hand, these breaks from tradition would reflect a failure to consider relevant and significant changes in how consumers shop for food and groceries in today's world.

The FTC has a long history of assessing retail mergers in a manner significantly at odds with the aggressive approach it is currently signaling. Only one supermarket merger has been challenged in court since American Store's acquisition of Lucky Stores in 1988: the Whole Foods/Wild Oats merger in 2007.[5] Over the last 35 years, the FTC has allowed every other supermarket merger and most retail-store transactions to proceed with divestitures. Within the last two years alone, these have

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[1] Press Release, *Kroger and Albertsons Companies Announce Definitive Merger Agreement*, KROGER (Oct. 14, 2022), https://ir.kroger.com/CorporateProfile/press-releases/press-release/2022/Kroger-and-Albertsons-Companies-Announce-Definitive-Merger-Agreement/default.aspx.

[2] In an article written with Sandeep Vaheesan before she became chair of the FTC, Lina Khan expressed disdain for grocery-industry consolidation and deep skepticism of even the best divestiture packages. *See* Lina Khan & Sandeep Vaheesan, *Market Power and Inequality: The Antitrust Counterrevolution and Its Discontents*, 11 HARV. L. & POL'Y REV. 235, 254 (2017) ("Retail consolidation has enabled firms to squeeze their suppliers… and led to worse outcomes for consumers.") & 289 ("Even if divestitures could be perfectly tailored and if they preserved competition in narrow markets in every instance, they would fail to advance the citizen interest standard.").

[3] *See, e.g.*, David Dayen, *Proposed Kroger-Albertsons Merger Would Create a Grocery Giant*, THE AMERICAN PROSPECT (Oct. 17, 2022), https://prospect.org/power/proposed-kroger-albertsons-merger-would-create-grocery-giant; Richard Smoley, *Kroger, Albertsons, and Lina Khan*, BLUE BOOK SERVICES (May 2, 2023), https://www.producebluebook.com/2023/05/02/kroger-albertsons-and-lina-khan.

[4] U.S. Dep't of Justice & Fed. Trade Comm'n, *Draft Merger Guidelines* (Jul. 19, 2023), *available at* https://www.justice.gov/d9/2023-07/2023-draft-merger-guidelines_0.pdf. *See also* Gus Hurwitz & Geoffrey Manne, *Antitrust Regulation by Intimidation*, WALL ST. J. (Jul. 24, 2023), https://www.wsj.com/articles/antitrust-regulation-by-intimidation-khan-kanter-case-law-courts-merger-27f610d9.

[5] Prior to Whole Foods/Wild Oats, the last litigated supermarket merger was the State of California's 1988 challenge to American Store's acquisition of Lucky Stores. Several *retail* mergers have been challenged in court, however, such as Staples/Office Depot in 2015. *See* Press Release, *FTC Challenges Proposed Merger of Staples, Inc. and Office Depot, Inc.*, FEDERAL TRADE COMMISSION (Dec. 7, 2015), https://www.ftc.gov/news-events/news/press-releases/2015/12/ftc-challenges-proposed-merger-staples-inc-office-depot-inc.

included Tractor Supply/Orschlein and 7-Eleven/Speedway.[6] The FTC's historic approach recognizes the reality that competitive concerns regarding supermarket mergers can be readily and adequately remedied by divestitures in geographic markets of concern; indeed, even Whole Foods/Wild Oats was ultimately resolved with a divestiture agreement following a fractured circuit court decision.[7]

The retail food and grocery landscape has changed dramatically since American/Lucky and Whole Foods/Wild Oats. But the ways in which the market has changed point toward its becoming more competitive, further undermining a possible FTC case. With the growth of wholesale clubs, delivery services, e-commerce, and other retail formats, the industry is no longer dominated by traditional supermarkets. In addition, these changing dynamics have made geographic distance, traffic patterns, and population density decreasingly relevant in a consumer's choice of where they purchase food and groceries. Today, Kroger is only the fourth-largest food and grocery retailer in the United States, behind Walmart, Amazon, and Costco. If the merger goes through, the combined firm will move into third place in market share but would still account for just 9% of nationwide sales.[8]

The upshot is that the food and grocery industry is arguably as competitive as it has ever been. Unfortunately, recent developments suggest the FTC may well ignore or dismiss the economic realities of this rapid transformation of the food and grocery industry, substituting instead the outdated approach to market definition and industry concentration signaled by the draft guidelines.[9]

In light of these developments in the food-retail market and the FTC's likely break from precedent, this paper highlights important areas where both the commission and commentators' stances appear to run headlong into legal precedent that mandates an evidence-based approach to merger review, even as the best available evidence points to a dynamic and competitive grocery industry. The correct understanding of the law and the industry appears entirely at odds with a challenge to the proposed merger.

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[6] This includes approving Albertsons/Safeway (2015), Ahold/Delhaize (2016), and Price Chopper/Tops (2022). *See* Analysis of Agreement Containing Consent Order to Aid Public Comment, *In the Matter of Cerberus Institutional Partners V, L.P., AB Acquisition, LLC, and Safeway Inc.* (File No. 141 0108) (Jan. 27, 2015) *available at* https://www.ftc.gov/system/files/documents/cases/150127cereberusfrn.pdf; Analysis of Agreement Containing Consent Order to Aid Public Comment, *In the Matter of Koninklijke Ahold N.V. and Delhaize Group NV/SA* (File No. 151-0175) (Jul. 22, 2016), *available at* https://www.ftc.gov/system/files/documents/cases/160722koninklijkeanalysis.pdf; Analysis of Agreement Containing Consent Order to Aid Public Comment, *In the Matter of The Golub Corporation and Tops Markets Corporation* (File No. 211-0002, Docket No. C-4753) (Nov. 8, 2021), *available at* https://www.ftc.gov/system/files/documents/cases/2110002pricechoppertopsaapc.pdf.

[7] Decision and Order, *In the Matter of Whole Foods Market, Inc.*, (Docket No. 9324) (May 28, 2009), *available at* https://www.ftc.gov/sites/default/files/documents/cases/2009/05/090529wfdo.pdf; *FTC v. Whole Foods Market*, 548 F.3d 1028 (D.C. Cir. 2008).

[8] Number based on authors' calculations, using data from *90th Annual Report*, PROGRESSIVE GROCER (May 2023), https://progressivegrocer.com/crossroads-progressive-grocers-90th-annual-report.

[9] *See Draft Merger Guidelines*, *supra* note 4.

A. The FTC's Merger-Enforcement Policy Is on a Collision Course with the Law

The Kroger/Albertsons merger proceeds against a backdrop of tough merger-enforcement rhetoric and actions from the FTC. Recent developments include the publication of aggressive revised merger guidelines, a string of cases brought to block seemingly benign mergers, process revisions that burden even unproblematic mergers, and FTC leadership's contentious and expansive interpretation of the merger laws. The FTC's ambition to remake U.S. merger law is likely to falter before the courts, but not before imposing a substantial tax on all corporate transactions—and, ultimately, on consumers.

The retail food and grocery market has changed substantially since the last time a supermarket merger was challenged in court. If the merger goes to trial, the court will need to address issues that have not been litigated in decades, if ever. Depending how the court rules, the market definition for future supermarket mergers may be substantially revised. Moreover, if the FTC attempts to litigate allegations of labor-market or input-market monopsony, the agency runs the risk of a humiliating loss that could stymie future attempts to expand the role of monopsony in competition enforcement and policy. The FTC thus would do well to even-handedly assess the Kroger Albertsons merger, remaining open to new evidence and sensible remedies. This is especially true given the agency's losing streak in court—culminating with its unsuccessful challenges of the *Meta/Within* and *Microsoft/Activision Blizzard* deals.[10]

B. The Product Market Is Broader Than Local Supermarkets

Because of recent changes in market dynamics, it no longer makes sense to limit the relevant market to supermarkets alone. Rather, consumer behavior in the face of omnipresent wholesale clubs, e-commerce, and local delivery platforms significantly constrains supermarkets' pricing decisions.

Recent FTC consent orders involving supermarket mergers have limited the relevant product market to local brick-and-mortar supermarkets and food and grocery sales at nearby hypermarkets (*e.g.*, Walmart supercenters), while excluding wholesale-club stores (*e.g.*, Costco), e-commerce (*e.g.*, Amazon), and further-flung stores accessible through online-delivery platforms (*e.g.*, Instacart). This is based on an assertion that the relevant market includes only those retail formats in which a consumer can purchase nearly all of a household's weekly food and grocery needs from a single stop, at a single retailer, in the shopper's neighborhood. This is, however, no longer how most of today's consumers shop. Instead, shoppers purchase different bundles of groceries from multiple sources,

[10] *FTC v. Meta Platforms Inc.*, U.S. Dist. LEXIS 29832 (2023); *FTC v. Microsoft Corporation et al.*, No. 23-cv-02880-JSC (N.D. Cal. Jul. 10, 2023), *available at* https://s3.documentcloud.org/documents/23870711/ftc-v-microsoft-preliminary-injunction-opinion.pdf.

often simultaneously.[11] This pattern has substantial implications for supermarkets' competitive environment, and underscores why the FTC should not rely on outdated market definitions.

Past FTC consent orders have defined the relevant geographic markets to be areas that range from a two- to ten-mile radius around each of the merging parties' supermarkets.[12] The radius depends on such factors as population density, traffic patterns, and the unique characteristics of each market. It would, however, be reasonable to expand the relevant geographic market when club stores are present, as these have a larger catchment area than supermarkets. Finally, the rapid growth of e-commerce and delivery services make distance, traffic patterns, and population density decreasingly relevant in a consumer's choice of where they purchase food and groceries. As with product-market definitions, this is a crucial empirical issue that should be evaluated in the FTC's merger review and any litigation.

C. Labor Monopsony Concerns Are Unlikely to Hold Up in Court

More than in any previous retail merger, opponents of the Kroger/Albertsons deal have raised the specter of potential monopsony power in labor markets. But these concerns reflect a manifestly unrealistic conception of labor-market competition. Fundamentally, the market for labor in the retail sector is extremely competitive, and workers have a wide range of alternative employment options—both in and out of the retail sector. At the same time, both Kroger and Albertsons are highly unionized, providing a counterbalance to any potential exercise of monopsony power by the merged firm.

D. The Alleged 'Waterbed Effect' Is Not Borne Out by Evidence

Some critics of the merger have speculated that the merged company would be able to exercise monopsony power against its food and grocery suppliers (*i.e.*, wholesalers and small manufacturers), often invoking an economic concept called the "waterbed effect." The intuition is that the largest buyers may use their monopsony power to negotiate lower input prices from suppliers, leading the suppliers to make up the lost revenue by raising prices for their smaller, weaker buyers.

But these arguments are far from compelling. It is very difficult, for example, to hypothesize any relevant market for purchasing a good where the merged firm would have market power. Critics also often fail to consider the ability of many producers—both small and large—to sell directly to consumers, as demonstrated by the rise of online shopping, with its low entry barriers entry and low-cost structure.

Much of the discussion of the waterbed effect focuses on harm to competing retailers, rather than consumers. But this is not the harm that U.S. antitrust law seeks to prevent. It is thus not surprising

[11] *See, e.g.*, George Kuhn, *Grocery Shopping Consumer Segmentation*, DRIVE RESEARCH (2002), *available at* https://www.driveresearch.com/media/4725/final-2022-grocery-segmentation-report.pdf.

[12] *See, e.g.*, *In the Matter of Cerberus Institutional Partners*, *supra* note 6, at 3.

that at least one U.S. court has rejected waterbed-effect claims on grounds that there was no harm to consumers.

E. Divestitures Historically Have Proven an Appropriate and Adequate Remedy

Historically, the FTC has allowed most grocery-store transactions to proceed with divestitures, such as Ahold/Delhaize (81 stores divested), Albertsons/Safeway (168 stores), and Price Chopper/Tops (12 stores). The extent of the remedies sought depends on the extent of post-merger competition in the relevant local markets, as well as the likelihood of significant entry by additional competitors into the relevant markets. The benefit of selling off stores is that you can allow the vast majority of stores—where there is no worry about anticompetitive effect—to merge, while targeting the areas that have the highest concern.

Despite a long history of divestitures serving as an appropriate and adequate remedy in supermarket mergers, some point to the Albertsons/Safeway merger divestitures to Haggen as evidence that divestitures are no longer an appropriate remedy. But several factors idiosyncratic to Haggen and its acquisition strategy led to the failure of that divestiture, and it does not properly stand for the claim that *all* supermarket divestitures are doomed.

In September 2023, Kroger and Albertsons announced a $1.9 billion divestiture proposal to sell 413 stores, eight distribution centers, two offices, and five private-label brands to C&S Wholesale Grocers LLC.[13] If consummated, the deal would cover operations spanning 17 states and the District of Columbia, and C&S has committed to maintain collective-bargaining agreements with labor.[14] As antitrust enforcers review whether these proposed divestitures are adequate, they should learn from the Haggen experience, rather than view it as justification to reject reasonable divestiture options that have worked for other mergers.

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[13] Press Release, *Kroger and Albertsons Companies Announce Comprehensive Divestiture Plan with C&S Wholesale Grocers, LLC in Connection with Proposed Merger*, THE KROGER CO. (Sep. 8, 2023), https://www.prnewswire.com/news-releases/kroger-and-albertsons-companies-announce-comprehensive-divestiture-plan-with-cs-wholesale-grocers-llc-in-connection-with-proposed-merger-301921933.html.

[14] *Id.*

I. Introduction

In October 2022, the Kroger Co. and Albertsons Cos. announced their intent to merge the two companies in a deal valued at $24.6 billion.[15] Kroger is the fourth-largest food and grocery retailer in the United States—behind Walmart, Amazon, and Costco—while Albertsons is fifth.[16] Both chains trail market-leading Walmart by a considerable margin. Kroger operates 2,726 stores under the Kroger, Harris Teeter, and Smith's banners, while Albertsons operates 2,278 stores under the Safeway, Albertsons, and Von's grocery banners.[17] By contrast, Walmart and Sam's Club combined store count is greater than 5,300, and the company's grocery revenue is more than twice that of Kroger and Albertsons *combined*.[18]

While the proposed Kroger/Albertsons merger is a large transaction in terms of dollar valuation and the combined firm would move into third place in market share, it would still account for just 9% of nationwide sales.[19] In some localities, the market share would be much larger, however, raising questions regarding whether the merger would increase Kroger/Albertson's monopoly power in those retail markets and convey monopsony power in wholesale markets and local labor markets. To address such questions, Kroger and Albertsons have announced a $1.9 billion divestiture proposal that would include the sale of 413 stores and eight distribution centers across 17 states to C&S Wholesale Grocers LLC.[20]

But given the Federal Trade Commission's (FTC) recent disposition toward proposed mergers and Chair Lina Khan's previous writings about food retail, it is widely expected that the FTC will not be satisfied with any remedy offers from the companies—including offers to divest stores—and will instead attempt to block the merger.[21] California Attorney General Rob Bonta has also signaled that he is likely to challenge the deal.[22] In anticipation, Kroger's chief executive officer announced that both companies are "committed to litigate" if the enforcers act to block the merger.[23]

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[15] *See* Press Release, *supra* note 1.

[16] Progressive Grocer, *supra* note 8.

[17] *Who Are the Top 10 Grocers in the United States?*, FOODINDUSTRY.COM (last visited Oct. 10, 2023), https://www.foodindustry.com/articles/top-10-grocers-in-the-united-states-2019.

[18] *Id.*

[19] Number based on authors' calculations, using data from Progressive Grocer Staff, *90th Annual Report*, PROGRESSIVE GROCER (May 2023), https://progressivegrocer.com/crossroads-progressive-grocers-90th-annual-report.

[20] Kroger, *supra* note 13.

[21] *See Khan & Vaheesan*, *supra* note 2.

[22] *See* Leah Nylen & Jeannette Neumann, *California Preparing Lawsuit to Block Merger of Kroger, Jewel Parent*, BLOOMBERG (Oct. 12, 2023), https://www.chicagobusiness.com/retail/california-preparing-lawsuit-block-kroger-albertsons-deal.

[23] Alexander Coolidge, *Report: Kroger CEO Is "Committed to Litigate" If FTC Regulators Fight Albertsons Merger*, CINCINNATI ENQUIRER (May 11, 2023), https://www.cincinnati.com/story/money/2023/05/11/kroger-commited-to-litigate-if-ftc-blocks-albertsons-deal/70206692007.

What can we expect of such a court battle? The precedent is slightly complicated. While several retail mergers have been challenged in court, including Staples/Office Depot in 2015[24] and Whole Foods/Wild Oats in 2007,[25] no supermarket mergers have been litigated since the State of California's 1988 challenge to American Store's acquisition of Lucky Stores.[26] Both the supermarket business and antitrust analysis have changed dramatically over the intervening 35 years. In this paper, we describe some of the changes that have occurred within food retail over the past 35 years, and how they should be addressed by the merging parties, the FTC, and—if litigated—by the courts.

As with most merger analysis, many of the most important questions hinge on a proper definition of the relevant market. The most obvious changes we have observed in food retail in recent decades, including the rise of wholesale club stores and e-commerce, are directly relevant to the question of market definition. The most recent FTC consent orders involving supermarket mergers defined the relevant product market to include "traditional" brick-and-mortar supermarkets, as well as food and grocery sales at hypermarkets (*e.g.*, Walmart supercenters), while excluding wholesale club stores (*e.g.*, Costco) and e-commerce (*e.g.*, Amazon and home-delivery services).[27] This is based on the longstanding assertion that the relevant market includes only those retail formats in which a consumer can purchase all or nearly all of their household's weekly food and grocery needs during a single stop at a single retailer.

Any attempt by the FTC to maintain this outdated market definition will likely be challenged in court. Research has shown that consumer behavior has changed over time, in that the typical consumer no longer makes once-a-week shopping trips to a single food and grocery retailer.[28] Instead, the typical consumer makes multiple weekly trips and multi-homes across several different retailers and retail formats. This change alone blurs the line between traditional supermarkets and other retail formats. The extent to which wholesale clubs, e-commerce, and delivery services should be included in the relevant market is a key empirical issue that surely will—and should—be evaluated in the FTC's merger review and any ensuing litigation.

Geographic market is also an issue. The most recent FTC consent orders have defined the relevant geographic markets to be areas that range from a two- to ten-mile radius surrounding each of the merging parties' supermarkets.[29] The radius depends on such factors as population density, traffic

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[24] Press Release, *FTC Challenges Proposed Merger of Staples, Inc. and Office Depot, Inc.*, FEDERAL TRADE COMMISSION (Dec. 7, 2015), https://www.ftc.gov/news-events/news/press-releases/2015/12/ftc-challenges-proposed-merger-staples-inc-office-depot-inc.

[25] Jesse Greenspan, *FTC To Challenge Whole Foods, Wild Oats Merger*, LAW360 (Jun. 5, 2007), https://www.law360.com/texas/articles/26191/ftc-to-challenge-whole-foods-wild-oats-merger.

[26] *State of Cal. v. American Stores Co.*, 872 F.2d 837 (9th Cir. 1989) (granting preliminary injunction).

[27] *See, e.g., In the Matter of Cerberus Institutional Partners*, *supra* note 6, at 2-3.

[28] *See, e.g.*, Food Marketing Institute & The Hartman Group, *Consumers' Weekly Grocery Shopping Trips in the United States from 2006 to 2022 (Average Weekly Trips per Household)*, STATISTA (May 2022), *available at* https://www.statista.com/statistics/251728/weekly-number-of-us-grocery-shopping-trips-per-household.

[29] *See, e.g., In the Matter of Cerberus Institutional Partners*, *supra* note 6, *at 3*.

patterns, and the unique characteristics of each market. That, too, needs revision. Based on academic research, industry surveys, and reports from companies that find club stores compete with supermarkets and have larger catchment areas, we conclude that it would be reasonable to expand the relevant geographic market when club stores are present. In addition, the rapid growth of e-commerce and delivery services make distance, traffic patterns, and population density decreasingly relevant in a consumer's choice of where they purchase food and groceries. As with product-market definition, this is a crucial empirical issue that should be evaluated in the FTC's merger review and any ensuing litigation.

More than in any previous retail merger, opponents of the Kroger/Albertsons merger have raised the specter of potential monopsony power in labor markets. We argue that these concerns are likely overblown and will be nearly impossible to demonstrate if the merger were to be litigated. Fundamentally, the market for labor in the retail sector is highly competitive, with workers having a wide range of alternative employment if a particular employer attempted to exploit any claimed monopsony power. In addition, both Kroger and Albertsons are highly unionized. Through their collective-bargaining agreements, unions exercise monopoly power in labor negotiations that likely counterbalances any attempted exercise of monopsony power by the merged firm.

Lastly, some critics of the merger have speculated that the merged company may have and exercise monopsony power among its food and grocery suppliers (*e.g.*, wholesalers and small manufacturers). In particular, critics invoke a concept colloquially called the "waterbed effect," where pushing input prices down for some retailers ends up raising the price for other retailers. Why prices are "pushed" down is not always clear in popular discussions, nor is it clear that it qualifies as an antitrust harm in any way. Being the easiest trading partner would also result in lower prices.

We conclude this may be the weakest argument raised in opposition to the merger. The United Kingdom has evaluated "waterbed effect" allegations in at least two supermarket mergers and found no evidence indicating any anticipated effects from the mergers on input prices that would harm consumers.[30] More importantly, much of the discussion of waterbed effects focuses on harm to competing retailers, rather than to consumers. At least one U.S. court has rejected waterbed-effect claims

[30] *Safeway Merger Report*, UK COMPETITION COMMISSION (2003), *available at* https://webarchive.nationalarchives.gov.uk/ukgwa/20120119163858/http:/www.competition-commission.org.uk/inquiries/completed/2003/safeway/index.htm ("Overall, therefore, there is little evidence of an immediate or short-term 'waterbed' effect. … [O]ur surveys produced insufficient evidence on this point for us to conclude that any waterbed effect would be exacerbated by any of the mergers."); *Anticipated Merger between J Sainsbury PLC and ASDA Group Ltd: Summary of Final Report*, UK COMPETITION & MARKETS AUTHORITY (Apr. 25, 2019), *available at* https://assets.publishing.service.gov.uk/media/5cc1434ee5274a467a8dd482/Executive_summary.pdf ("Overall, it seems unlikely that many retailers will raise their prices in response to the Merger; and even if some individual retailers do, the overall effect on UK households is unlikely to be negative. On that basis, our finding is that the Merger is unlikely to lead to customer harm through a waterbed effect.").

on the grounds that (1) the plaintiffs did not demonstrate any harm to consumers, and (2) firms can substitute to other suppliers, thereby mitigating any anticipated waterbed effect.[31]

Given the size of a merged Kroger and Albertsons, it would be easy, but naïve, to conclude that the merger should be blocked.[32] The retail food and grocery market has changed substantially since the last time a supermarket merger was challenged in court. If the merger goes to trial, the court will address issues that have not been litigated in decades, if ever. Depending how the court rules, the market definition for future supermarket mergers may be substantially revised. Moreover, if the FTC attempts to litigate allegations of labor-market or input-market monopsony, the agency runs the risk of a humiliating loss that could stymie future attempts to expand the role of monopsony in competition enforcement and policy.

II. The Agencies Are Trying to Rewrite Merger-Review Standards

The recently published FTC-DOJ draft merger guidelines are a particularly notable backdrop for the Kroger/Albertsons merger, leading many commentators to expect the FTC to take a hardline stance on the deal.[33] Merger *case law*, however, has not changed much in recent years. Given the merging parties' apparent willingness to litigate the case, if necessary, the likelihood of a protracted legal battle appears to be high. As we explain below, at least at first sight, any case against the merger would be largely built on sand, and the commission's chances of succeeding in court appear slim.

The Clayton Act of 1914 grants the U.S. government authority to review and challenge mergers that may substantially lessen competition. The FTC and DOJ are the two antitrust agencies that share responsibility to enforce this law. Traditionally, the FTC investigates retail mergers, while the DOJ oversees other sectors, such as telecommunications, banking, and transportation.

Before the FTC and DOJ officials appointed by the current administration came into office, the settled practice was for the antitrust agencies to follow the 2010 Horizontal Merger Guidelines, which outline the analytical framework and evidence they use to evaluate mergers. The 2010 guidelines describe four major steps of merger analysis:

1. The first step is to define the relevant product and geographic markets affected by the merger. The goal is to identify the set of products and regions that are close substitutes to the merging parties' products and regions.
2. The second step is to assess the merger's competitive effects, or how the merger may harm competition in the defined markets.

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[31] *DeHoog v. Anheuser-Busch InBev, SA/NV,* No. 1:15-CV-02250-CL, 2016 U.S. Dist. LEXIS 137759, at *13-16 (D. Or. July 22, 2016).

[32] Leading to truculent statements like that of California Attorney General Rob Bonta that "[r]ight now, there's not a lot of reason not to sue [to block the merger]." *See* Nylen & Neumann, *supra* note 22.

[33] *See, e.g.*, Dayen, *supra* note 3; Smoley, *id*.

3. The third step is to examine the role of market entry as a potential counterbalance to the merger's competitive effects. For entry to be sufficient to deter or undo the anticompetitive effects of a merger, it must be timely, likely, and sufficient in scale and scope.
4. The fourth and final step is to evaluate the efficiencies the merger would generate, or how the merger may benefit consumers by reducing costs and improving quality.

The antitrust agencies weigh all these factors to determine whether a merger is likely to harm competition and consumers. If they find that a merger raises significant competitive concerns, they may seek to block it or require remedies such as divestitures or behavioral commitments from the merging parties.

Several factors, however, suggest that authorities are unlikely to follow this measured approach when reviewing the Kroger/Albertsons merger. Primarily, the FTC and DOJ have recently issued draft revised merger guidelines. The 2023 guidelines have not yet been adopted, although the public comment period is closed. Compared to the previous iteration, which guided recent consent decrees, the new guidelines contain more stringent structural presumptions—that is, a presumption that a merger that merely increases concentration (as all horizontal mergers do) by a certain amount violates the law, rather than deferring to more nuanced economic analysis connecting specific market attributes to a likelihood of actual consumer harm.[34] These new, more stringent structural presumptions are not justified by new economic learnings about the economic effects of concentration. As now-FTC Bureau of Economics Director Aviv Nevo and colleagues wrote in 2022 (just before he joined the commission):

> If the agencies were to substantially change the presumption thresholds, they would also need to persuade courts that the new thresholds were at the right level. *Is the evidence there to do so? The existing body of research on this question is, today, thin and mostly based on individual case studies in a handful of industries. Our reading of the literature is that it is not clear and persuasive enough, at this point in time, to support a substantially different threshold that will be applied across the board to all industries and market conditions.*[35]

Although elements of Nevo and coauthors' proposed framework are present in the new proposed guidelines, the guidelines also incorporate new language that reflects a persistent thumb on the scale, systematically undermining merging parties' ability to justify their merger. For example, while a presumption of harm is triggered at a certain level of concentration (an HHI of 1800), in markets where there has previously been consolidation (over an unspecified timeframe), an impermissible "trend [toward concentration] can be established by… a steadily increasing HHI [that] exceeds 1,000 and

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[34] For instance, the Herfindahl–Hirschman Index (HHI) at which mergers are deemed problematic has been lowered from 2500 (and a post-merger increase of 200) to 1800 (and a post-merger increase of 100). Likewise, combined market shares of more than 30% are generally deemed problematic under the new guidelines (if a merger also increase the market's HHI by 100 or more). The revised guidelines also focus more heavily on monopsony and labor-market issues. *See Draft Merger Guidelines*, *supra* note 4, at 6-7.

[35] John Asker *et al*, *Comments on the January 2022 DOJ and FTC RFI on Merger Enforcement*, *available at* https://www.regulations.gov/comment/FTC-2022-0003-1847 at 15-16 (emphasis added).

rises toward 1,800."[36] Traditionally, an HHI under 1500 would be considered "unconcentrated" and presumed to raise no competitive concerns.[37]

While the FTC will likely point to the renewed focus on concentration measures as capturing the Clayton Act's focus on lessening competition and the tendency to create a monopoly, the draft guidelines make clear that commission now views concentration as problematic in itself, regardless of whether it lessens competition. For example, the draft guidelines state "efficiencies are not cognizable if they will accelerate a trend toward concentration."[38] Such a statement effectively negates any efficiency defense available to all but the very smallest firms. Efficiencies will almost always increase concentration—especially if those efficiencies come from economies of scale. If a merger creates efficiencies, the merged firm can lower costs, cut prices, and attract more customers. Attracting more customers with better products and prices will likely increase competition.

The economic evidence is quite strong that efficiency increases concentration.[39] If no efficiency defense is possible, any horizontal merger could accelerate a trend toward concentration (if it had been previously becoming more concentrated). Spinning in these circles is why the notion of a "trend" toward concentration raising particular concern hasn't been reflected in guidelines since 1968,[40] and reached its apotheosis in *Von's Grocery* in 1966[41]—one of the most thoroughly reviled merger cases in U.S. history.[42]

Before updating the merger guidelines, the FTC had already started to tighten its merger-enforcement policy. Among other actions, the agency brought high-profile cases against the *Illumina/GRAIL*, *Meta/Within*, and *Microsoft/Activision Blizzard* deals.[43] So far, all three challenges have resulted in defeat for the FTC in adjudication. Taken together, these cases suggest the agency is willing to push the law beyond its limits in an attempt to limit corporate consolidation, whatever the actual competitive effect. The courts have thus far shown themselves unwilling to buy the agencies more speculative claims of harm. In contrast, the DOJ recently was able to block Penguin-Random House from merging with Simon & Schuster.[44] On the surface, this may seem like a novel case

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[36] *Draft Merger Guidelines*, *supra* note 4, at 21.

[37] *See* U.S. Dep't of Justice & Fed. Trade Comm'n, *2010 Horizontal Merger Guidelines* (Aug. 19, 2010) at §5.3, *available at* https://www.justice.gov/atr/horizontal-merger-guidelines-08192010#5c.

[38] *Draft Merger Guidelines*, *supra* note 4, at 26.

[39] Chad Syverson, *Macroeconomics and Market Power: Context, Implications, and Open Questions* 33 J. ECON. PERSP. 23, 27 (2019).

[40] *See* U.S. Dep't of Justice, *Merger Guidelines* (1968) at 6-7, *available at* https://www.justice.gov/archives/atr/1968-merger-guidelines.

[41] *United States v. Von's Grocery Co.*, 384 U.S. 270 (1966).

[42] *See, e.g.*, Robert H. Bork, *The Goals of Antitrust Policy*, 57 AM. ECON. REV. PAPERS & PROCEEDINGS 242 (1967) ("In the *Von's Grocery* case a majority of the Supreme Court was willing to outlaw a merger which did not conceivably threaten consumers in order to help preserve small groceries in the Los Angeles area against the superior efficiency of the chains.").

[43] *Supra* note 10; *FTC v. Illumina, Inc.*, U.S. Dist. LEXIS 75172 (2021).

[44] *United States v. Bertelsmann SE & Co. KGaA, No. CV* 21-2886-FYP, 2022 WL 16949715 (D.D.C. Nov. 15, 2022).

similar to those the FTC has been pursuing; it involved monopsony power against authors. But in this case, the parties agreed that, if there was harm to the authors, there would be fewer books, thereby harming consumers.[45] Fighting over harms to consumers (not concentration) is textbook antitrust litigation.[46]

Finally, the FTC's leadership has been particularly bearish about the potential consumer benefits of corporate mergers and acquisitions. This inclination is reflected in Chair Khan's assertion that the Clayton Act embodies a "broad mandate aimed at prohibiting mergers even when they do not constitute monopolization and even when their tendency to lessen competition is not certain."[47] One way to prohibit mergers is to make them more costly without even going to court. This is what will happen under the agencies' proposed changes to the premerger notification rules ("Hart-Scott-Rodino Act").[48] Despite no evidence presented of anticompetitive mergers slipping through the cracks due to the current reporting being too lax, the revised guidelines would greatly increase the cost of merging, thereby reducing the number of mergers.

Even the FTC estimates a massive increase in compliance costs of approximately $350 million, to more than $470 million per year. But that estimate is likely a serious underestimate, as it is based on, among other things, an unscientific "estimate" of the time involved and a dated assumption about the average hourly costs imposed on filers' senior executives and firms' counsel.

A survey that the U.S. Chamber of Commerce conducted of 70 antitrust practitioners about the proposed HSR revisions found that the new rules would increase compliance costs by $1.66 billion, almost five times the FTC's $350 million estimate."[49] While this general approach to blocking more mergers will not be directly applicable in any particular case, it highlights the FTC's willingness to not follow "the old rules."

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[45] *Id.* ("The defendants do not dispute that if advances are significantly decreased, some authors will not be able to write, resulting in fewer books being published, less variety in the marketplace of ideas, and an inevitable loss of intellectual and creative output.")

[46] Brian Albrecht, *Business as Usual for Antitrust*, CITY JOURNAL (Nov 22, 2022), *available at* https://www.city-journal.org/article/business-as-usual-for-antitrust.

[47] Lina M. Khan, Rohit Chopra, & Kelly Slaughter, Comm'rs, FED. TRADE COMM'N, *Statement on the Withdrawal of the Vertical Merger Guidelines* (Sep. 15, 2021) at 3, *available at* https://www.ftc.gov/system/files/documents/public_statements/1596396/statement_of_chair_lina_m_khan_commissioner_rohit_chopra_and_commissioner_rebecca_kelly_slaughter_on.pdf.

[48] *Premerger Notification Rules*, 88 FED. REG. 42178 (RIN 3084-AB46), proposed Jun. 29, 2023 (to be codified at 16 C.F.R. Parts 801 and 803).

[49] *Antitrust Experts Reject FTC/DOJ Changes to Merger Process,* U.S. CHAMBER OF COMMERCE (Sep. 19, 2023), https://www.uschamber.com/finance/antitrust/antitrust-experts-reject-ftc-doj-changes-to-merger-process. The surveyed group was made up seasoned antitrust veterans from across a variety of backgrounds: 80% had been involved in more than 50 mergers and 59% in more than 100.

All of these factors—in concert with the merging parties' claim that they are prepared to go to court if the FTC decides to block the transaction outright[50]—suggest that there is a particularly high likelihood that the Kroger/Albertsons merger will be challenged and litigated, rather than approved, or challenged and settled.

For the reasons outlined in the following sections, however, the FTC is unlikely to prevail in court. The market overlaps between the merging parties are few and can be resolved by relatively straightforward divestiture remedies, as already proposed by the parties—which, even if disfavored by the agency, are routinely accepted by courts. Likewise, the FTC's likely market definition and potential theories of harm pertaining to labor monopsony and purchasing power more generally appear speculative at best. The upshot is that the FTC's desire to bring tougher merger enforcement appears to be on a collision course with the law as it is currently enforced by U.S. courts.

III. The Relevant Market Is Broader Than Hyper-Local Supermarkets

The retail food and grocery landscape has changed dramatically since the last litigated supermarket merger. Consumer-shopping behavior has shifted toward more frequent shopping trips across a wide variety of formats, which include warehouse clubs (*e.g.*, Costco); e-commerce (*e.g.*, Amazon); online-delivery platforms (*e.g.*, Instacart); limited-assortment stores (*e.g.*, Trader Joe's and Aldi); natural and organic markets (*e.g.*, Whole Foods); and ethnic-specialty stores (*e.g.*, H Mart); in addition to traditional supermarkets. Because of these enormous changes, the market definition assumed in previous FTC consent orders likely will be—and should be—challenged, given the empirical evidence.

A. Recent Trends in Retailing Have Upended the 'Traditional' Grocery Market Definition

The FTC is likely to find the relevant product market to be *supermarkets*, which the agency has previously defined as retail stores that enable consumers to purchase all of their weekly food and grocery requirements during a single shopping visit. This product-market definition has remained mostly unchanged for at least a quarter of a century. In both the Albertsons/Safeway merger and the Ahold/Delhaize merger, consent orders between the FTC and the merging parties defined the relevant market to be "the retail sale of food and other grocery products in supermarkets."[51] The orders defined supermarkets as "full-line grocery stores" that provide "one-stop shopping" that enables consumers "to shop in a single store for all of their food and grocery needs."[52]

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[50] *Supra* note 23.

[51] Analysis of Agreement Containing Consent Order to Aid Public Comment, *In the Matter of Cerberus Institutional Partners V, L.P., AB Acquisition, LLC, and Safeway Inc.* (File No. 141 0108) (Jan. 27, 2015) *available at* https://www.ftc.gov/system/files/documents/cases/150127cereberusfrn.pdf. Analysis of Agreement Containing Consent Order to Aid Public Comment, *In the Matter of Koninklijke Ahold N.V. and Delhaize Group NV/SA* (Jul. 22, 2016) (File No. 151-0175) *available at* https://www.ftc.gov/system/files/documents/cases/160722koninklijkeanalysis.pdf.

[52] *In the Matter of Cerberus Institutional Partners*, *supra* note 6, at 2.

On the one hand, the consent orders' product-market definitions included supermarkets located within hypermarkets, such as Walmart supercenters. Hypermarkets sell both products that are not typically sold in traditional supermarkets, as well as a sufficient range of food and grocery products such that consumers can "purchase all of their weekly grocery requirements in a single shopping visit."[53]

On the other hand, the consent orders excluded club stores—such as Costco, Sam's Club, and BJ's Wholesale Club—as well as "hard discounters, limited assortment stores, natural and organic markets, [and] ethnic specialty stores."[54] The orders claim that these stores are excluded from the relevant product market because "they offer a more limited range of products and services than supermarkets and because they appeal to a distinct customer type."[55] In addition, the orders indicate that "supermarkets do not view them as providing as significant or close competition as traditional supermarkets."[56] Prior consent orders omitted any discussion of whether online retailers or delivery services should be included or excluded from the relevant market. This product-market definition has remained mostly unchanged—and mostly unchallenged—since the Ahold/Giant merger a quarter-century ago.[57]

Figure 1 shows that retail sales by supermarkets, warehouse clubs, supercenters, and other grocery stores have been relatively stable at 5-6% of U.S. gross domestic product (GDP).[58] Figure 2 shows that supermarkets' share of retail sales dropped sharply from the early 1990s through the mid-2000s, with that share shifting to warehouse clubs and supercenters. These figures are consistent with the conclusion that warehouse clubs and supercenters successfully compete against traditional grocery stores. Indeed, it would be reasonable to conclude that the rise of warehouse clubs and supercenters at the expense of traditional supermarkets is one of the most significant long-run trends in retail.

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[53] In this paper, the terms "hypermarket" and "supercenter" are used synonymously. *See* Richard Volpe, Annemarie Kuhns, & Ted Jaenicke, *Store Formats and Patterns in Household Grocery Purchases*, Economic Research Service Economic Information Bulletin No. 167 (Mar. 2017), https://www.ers.usda.gov/webdocs/publications/82929/eib-167.pdf?v=0 (supercenters are also known as hypermarkets or superstores).

[54] *In the Matter of Cerberus Institutional Partners*, *supra* note 6, at 3.

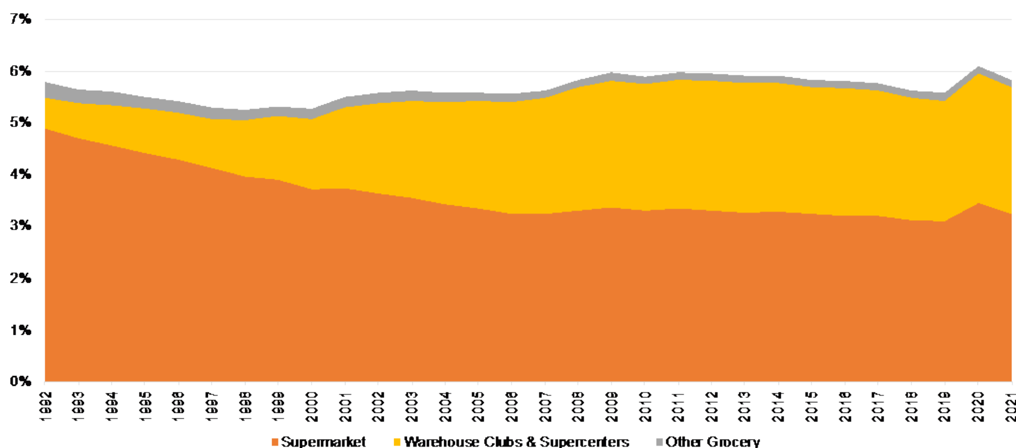
[55] *Id.*

[56] *Id.*

[57] *See In the Matter of Koninklijke Ahold*, *supra* note 6.

[58] Data obtained from: U.S. Census Bureau, *Report on Retail Sales and Trends: Annual Retail Trade Survey: 2021*, https://www.census.gov/data/tables/2021/econ/arts/annual-report.html.

FIGURE 1: U.S. Retail Sales as Percentage of GDP by Kind of Business, 1992-2021



SOURCE: *U.S. Census Bureau, Annual Retail Trade Survey*

The retail food and grocery industry has changed dramatically. In particular, a great deal of attention has been paid to consolidation in the industry. Lina Khan & Sandeep Vaheesan, for example, note that "[t]he share of groceries sold by the four biggest food retailers more than doubled between 1997 and 2009, from seventeen percent in 1994 to twenty-eight percent in 1999 and thirty-four percent in 2004."[59]

Below, we note that the average consumer shops for food and groceries more than once a week and shops at more than one retail format in a given week. Competition in groceries is not just between supermarkets. While Khan & Vaheesan recognize that supermarkets started to compete with warehouse clubs and supercenters, they fail to update their market definition to reflect that competition.[60] Over the period of increasing concentration within groceries, warehouse clubs and supercenters were steadily eroding supermarkets' share of retail sales.

Figure 2 shows that, in 1994, supermarkets accounted for 81% of retail sales, which fell to 61% by 2004.[61] Over the same period warehouse clubs and supercenters grew from 14% of retail sales to 35%. In 2021, supermarkets accounted for 56% of retail sales and warehouse clubs and supercenters accounted for 42%. Since the Ahold/Giant merger in 1998, warehouse clubs and supercenters have doubled their share of retail sales, while supermarkets' share has dropped by more than 25%.[62] Put simply, the four largest supermarket retailers were occupying a larger share of a shrinking segment.

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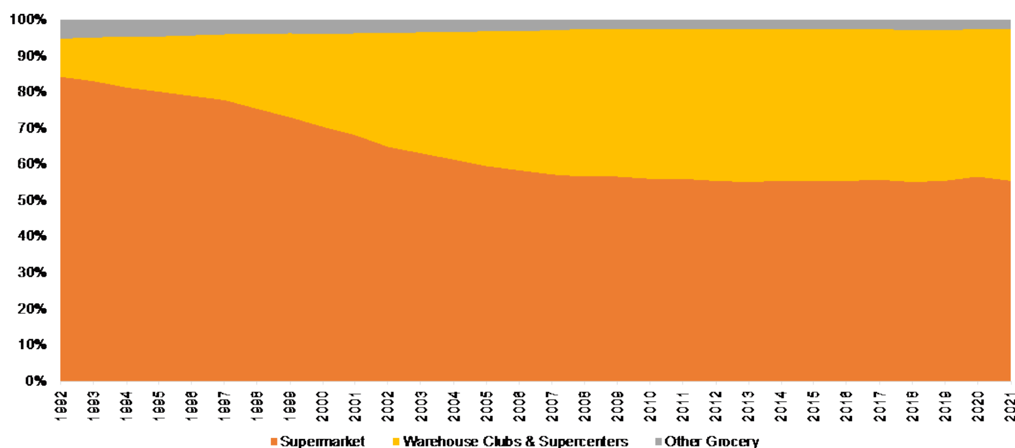
[59] Khan & Vaheesan, *supra* note 2, at 255.

[60] *Id.* ("Grocers sought to bulk up in order to compete with the scale of warehouse clubs and large discount stores, fueling further mergers and leading many local grocers to close….").

[61] U.S. Census Bureau, *supra* note 58.

[62] *Id.*

FIGURE 2: U.S. Retail Sales Share by Kind of Business, 1992-2021



SOURCE: *U.S. Census Bureau, Annual Retail Trade Survey*

Based on these observations, the product-market definition that the FTC has employed in its consent orders over the past more than two decades is likely to be—and should be—challenged to include warehouse clubs, in addition to accounting for online retail and delivery.

B. The Once-a-Week Shopper Is No Longer the Norm

In the past, the FTC has specified that, for a firm to be in the relevant market of "supermarkets," it must be able to "enable[e] consumers to purchase substantially all of their weekly food and grocery shopping requirements in a single shopping visit."[63] This definition suffers from several deficiencies.

The first deficiency is that this hypothetical consumer behavior is at odds with how many or most consumers behave today.

- Surveys conducted by the Food Marketing Institute and The Hartman Group report the average shopper makes 1.6 weekly trips to buy groceries.[64]
- Earlier research by FMI and Hartman find, in addition, other household members take another 0.6 trips, implying that the total number of trips per household each week is about 2.2, or approximately one trip every three days.[65]
- Surveys conducted by Drive Research show the average household makes an average of 8.1 grocery shopping trips a month, or around two trips a week (Table 1).[66]

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[63] *In the Matter of Cerberus Institutional Partners*, *supra* note 6, at 2.

[64] Food Marketing Institute & The Hartman Group, *Consumers' Weekly Grocery Shopping Trips in the United States from 2006 to 2022 (Average Weekly Trips per Household)*, STATISTA (May 2022), *available at* https://www.statista.com/statistics/251728/weekly-number-of-us-grocery-shopping-trips-per-household.

[65] Michael Browne, *Grocery Shopping Has a Hold on Consumers, Study Finds*, SUPERMARKET NEWS (Jun. 27, 2018), https://www.supermarketnews.com/issues-trends/grocery-shopping-has-hold-consumers-study-finds.

[66] Kuhn, *supra* note 1111.

TABLE I: Grocery Shopping Behavior by Consumer Segment

Segment	Number	Percent	Trips per Month	Avg. Spend per Trip	Avg. Spend per Month	Grocery	Mass Merch.	Club	Local Ind. Grocery	Natural / Spec. Grocery	Dollar	Online Retailer
Seasoned planners	182	16%	5	$125	$625	70%	47%	24%	18%	20%		
Frugal do-it-yourselfers	133	12%	6	116	696	70%	59%	21%	23%		21%	
Health-conscious families	78	7%	12	173	2,076	59%	62%		33%	51%		40%
Grocery enthusiasts	150	14%	8	162	1,296	57%	63%	25%	23%		23%	
Anti-shoppers	94	8%	5	135	675	56%	46%				19%	29%
Simple pleasure seekers	162	15%	8	137	1,096	54%	62%	16%	22%		25%	
Young spenders	305	28%	11	200	2,200	38%	50%	24%			27%	27%
Total / Average	**1,104**	**100%**	**8.1**	**$164**	**$1,336**	**55%**	**55%**	**19%**	**14%**	**7%**	**19%**	**13%**

SOURCE: *Drive Research*

There is no evidence that consumers view retailers that provide one-stop shopping for an entire week's food and grocery needs as distinct from other retailers who provide food and groceries. In fact, evidence suggests that many consumers "multi-home" across several different retail categories.

- Survey data published by Drive Research indicate that many households spread their shopping across grocery stores, mass merchants, warehouse clubs, independent grocery stores, natural and specialty grocery stores, dollar stores, and online retailers (Table 1).[67]
- Acosta, a sales and marketing consulting firm, reports that 76% of consumers shop at more than one retailer a week and about one third "retail hop" among three or more retailers a week for groceries and staples.[68]
- Research from the University of Florida found that, in 2017, an average consumer visited 3.2 to 4.3 different formats of food outlets a month, depending on income level.[69]
- Survey results from PYMNTS, a data-analysis firm, demonstrate a significant shift in consumer spending away from traditional supermarkets. For example, in 2020, approximately 98% of consumers who bought at least one common household product each week—"center aisle" products, such as paper towels, cleaning supplies, and canned goods—made the purchase at a grocery store. In 2023, more than a third of consumers (37%) say they purchase *none* of these products from a traditional grocery store, with online purchases accounting for much of the shift.[70]

Thus, while one-stop weekly food and grocery shopping at single retailers was once typical, the evidence indicates such a phenomenon is much less common today.

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[67] *Id.*

[68] *Trip Drivers: Top Influencers Driving Shopper Traffic*, ACOSTA (2017), *available at* https://acostastorage.blob.core.windows.net/uploads/prod/newsroom/publication_phetw_0rzq.pdf.

[69] Lijun Angelia Chen & Lisa House, *US Food Shopper Trends in 2017*, UNIV. OF FLA, IFAS Extension Pub. No. FE1126 (Dec. 7, 2022), https://edis.ifas.ufl.edu/publication/FE1126.

[70] Karen Webster, *Consumer Shopping Data Shows Troubling Signs for Grocery Stores' Future*, PYMNTS (Feb. 6, 2023), https://www.pymnts.com/news/retail/2023/consumer-shopping-data-shows-troubling-signs-for-grocery-stores-future.

C. Supermarkets Compete with Warehouse Clubs

The FTC's earlier consent orders provide four reasons to exclude warehouse clubs from the relevant market that includes supermarkets:

1. They offer a "more limited range of products and services" than supermarkets;
2. They "appeal to a distinct customer type" from supermarket customers;
3. Shoppers do not view warehouse clubs as "adequate substitutes for supermarkets;" and
4. Supermarkets do not view warehouse clubs as "significant or close competition," relative to other supermarkets.[71]

In contrast to these conclusions, there is widespread recognition today that warehouse clubs impose significant competitive pressure on supermarkets.[72]

- The National Academies of Sciences concludes that, over time, the entry and growth of warehouse clubs, superstores, and online retail has "blurred" the distinctions among retail formats.[73] More importantly for merger-review analysis, the National Academies concludes that the retail sector is "highly competitive," in part because of the entry and growth of warehouse clubs, superstores, and online retail.[74]
- Based on their empirical analysis, Paul Ellickson and coauthors conclude that warehouse clubs are "relevant substitutes" for supermarkets, even when the club stores are outside the geographic area typically used by the FTC in merger reviews.[75]
- Prior to her appointment as FTC chair, Lina Khan and her coauthor concluded that competition from warehouse clubs "fueled" grocery mergers in the late 1990s.[76]

The FTC's consent orders note that warehouse clubs offer a "more limited range of products and services" than supermarkets. The orders identify products sold at supermarket as "including, but not

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[71] *See, e.g., In the Matter of Cerberus Institutional Partners*, *supra* note 6, at 3.

[72] *See* Paul B. Ellickson, Paul L.E. Grieco, & Oleksii Khvastunov, *Measuring Competition in Spatial Retail*, 51 RAND J. ECON. 189 (2020) ("[C]lub stores are able to draw revenue from a significantly larger geographic area than traditional grocers. Hence, club stores are relevant substitutes for grocery stores, even if they are located even several miles away, a fact that could easily be overlooked in an analysis in which stores are simply clustered by geographic market.").

[73] NATIONAL ACADEMIES OF SCIENCES, ENGINEERING, AND MEDICINE, A SATELLITE ACCOUNT TO MEASURE THE RETAIL TRANSFORMATION: ORGANIZATIONAL, CONCEPTUAL, AND DATA FOUNDATIONS (2021), *available at* https://www.bls.gov/evaluation/a-satellite-account-to-measure-the-retail-transformation.pdf ("[T]he restructuring that started first with the warehouse clubs and superstores and then moved on to e-commerce has begun to blur the lines between the retail industry and several other sectors....").

[74] *Id.* at 25 ("[C]hanges experienced by retail over the past few decades suggest that the sector is highly competitive and is undergoing substantial change and reorganization. As discussed earlier, the changes described involve warehouse clubs and superstores ... e-commerce ... digital goods, imports, and large firms....").

[75] Ellickson *et al.*, *supra* note 72, ("Due to their size and attractiveness for larger purchases, club stores represent strong competitors to grocery stores even, when they are a significant distance away.").

[76] Khan & Vaheesan, *supra* note 2, at 255 ("Grocers sought to bulk up in order to compete with the scale of warehouse clubs and large discount stores, fueling further mergers and leading many local grocers to close....").

limited to, fresh meat, dairy products, frozen foods, beverages, bakery goods, dry groceries, detergents, and health and beauty products."[77]

The annual reports for Costco, Walmart (which include Sam's Club), and BJ's, however, indicate that each company offers the same range of products the FTC consent orders identify as being offered by supermarkets.[78] Indeed, the reports indicate that supermarkets do consider wholesale clubs to be competitors and *vice versa*. BJ's annual report goes to great lengths to explain its efforts to compete with supermarkets by offering similar manufacturer-branded products at lower prices.[79] The role of warehouse clubs cannot be assumed or asserted away. Indeed, any identification of the relevant market for retail food and grocery sales should begin with a presumption that warehouse clubs provide competitive pressure, since that is what the economics research finds.

It is true that warehouse stores typically carry fewer stock-keeping units ("SKUs") than supermarkets. Costco's annual report indicates the company carries fewer than 4,000 SKUs in its warehouse stores and offers 10,000 to 11,000 SKUs for online purchases.[80] BJ's annual report says that the company carries "approximately 7,000 core active stock keeping units."[81] In contrast, the BJ's report notes, "supermarkets normally carry an average of 40,000 SKUs, and supercenters may stock 100,000 SKUs or more." But these differences in SKU counts do not in themselves demonstrate fundamental differences in product offerings between the two store formats.[82]

The main difference between the two formats is that warehouse clubs tend to offer a smaller range of sizes and packaging and a smaller variety of brands. For example, Costco notes that many of the products it stocks "are offered for sale in case, carton, or multiple-pack quantities only."[83] Another difference can be observed in the variety of brands offered. For example, Costco has invested in developing its Costco Wholesale and Kirkland Signature private labels.[84] In contrast, CFRA Research analyst Arun Sundaram observes that Sam's Club "typically offers a bigger national-brand

[77] *See, e.g., In the Matter of Cerberus Institutional Partners*, *supra* note 6, at 2.

[78] Costco Wholesale Corporation, Annual Report (Form 10-K) (Aug. 28, 2022), https://www.sec.gov/ix?doc=/Archives/edgar/data/0000909832/000090983222000021/cost-20220828.htm; BJ's Wholesale Club Holdings, Inc., Annual Report (Form 10-K) (Mar. 16, 2023), https://www.sec.gov/ix?doc=/Archives/edgar/data/1531152/000153115223000026/bj-20230128.htm; Walmart Inc., Annual Report (Form 10-K) (Mar. 27, 2023), https://www.sec.gov/ix?doc=/Archives/edgar/data/104169/000010416923000020/wmt-20230131.htm.

[79] BJ's Wholesale Club Holdings, Inc, *id.*

[80] Costco Wholesale Corporation, *id.*

[81] BJ's Wholesale Club Holdings, Inc, *id.*

[82] *Id.*

[83] Costco Wholesale Corporation, *id.*

[84] *Id.*

product selection than its club cohorts."[85] Such differences are insufficient to exclude wholesale clubs from the relevant market. If warehouse clubs offer similar products, see themselves as competing with supermarkets, and customers view them as substitutes, warehouse clubs must be in the same market.

D. E-Commerce Has Changed the Food Landscape

In the years since the Ahold/Giant merger in 1998, online shopping and home delivery have grown from niche services serving only 10,000 households nationwide to a landscape where approximately one-in-eight consumers purchase groceries "exclusively" or "mostly" online.[86] This shift has increased competition and innovation in the supermarket industry, as traditional supermarkets have adapted to changing consumer preferences and behaviors by offering more delivery and pickup options, expanding their online assortments, and enhancing their digital capabilities.[87] Some have invested in their own e-commerce platforms and many have partnered with such third-party providers as Instacart, Shipt, and Peapod.[88]

One might surmise that e-commerce simply replaced in-person shopping, but with the same stores competing. This is not what has been observed. E-commerce has also increased competition by bringing in new companies with which traditional stores need to compete (*e.g.*, Amazon) and by increasing the options available to consumers through services like Instacart, which allow for direct price and product comparisons among many stores. Each of these innovations has blurred the lines between brick-and-mortar food and grocery retailers and e-commerce, as well as the lines between supermarkets and other retail formats.

In 2023, more than a third of consumers (37%) say they purchase no center-aisle products (products such as paper towels, cleaning supplies, and canned goods) from a traditional grocery store, with online purchases accounting for much of the shift.[89] The fluidity between supermarkets, grocery stores, and online purchases makes the distinction nearly meaningless.

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[85] Russell Redman, *Report: Club Stores Absorbing Grocery Market Share from Supermarkets*, WINSIGHT GROCERY BUSINESS (Apr. 20, 2023), https://www.winsightgrocerybusiness.com/retailers/report-club-stores-absorbing-grocery-market-share-supermarkets.

[86] Hean Tat Keh & Elain Shieh, *Online Grocery Retailing: Success Factors and Potential Pitfalls*, 44 BUS. HORIZONS 73 (Jul.-Aug., 2001); Appinio & Spryker, *Share of Consumers Purchasing Groceries Online in the United States in 2022, by Channel*, STATISTA (Sep. 2002).

[87] *Navigating the Market Headwinds: The State of Grocery Retail* 2022, MCKINSEY & CO. (May 2022), *available at* https://www.mckinsey.com/~/media/mckinsey/industries/retail/how%20we%20help%20clients/the%20state%20of%20grocery%20retail%202022%20north%20america/mck_state%20of%20grocery%20na_fullreport_v9.pdf.

[88] *Id.*; Dimitri Dimitropoulos, Renée M. Duplantis, & Loren K. Smith, *Trends in Consumer Shopping Behavior and Their Implications for Retail Grocery Merger Reviews*, CPI ANTITRUST CHRON. (Dec. 2021), *available at* https://www.brattle.com/wp-content/uploads/2022/01/Trends-in-Consumer-Shopping-Behavior-and-their-Implications-for-Retail-Grocery-Merger-Review.pdf.

[89] *See* Webster, *supra* note 7070.

If a consumer uses Instacart to purchase and deliver groceries from Safeway, is that a supermarket purchase or e-commerce? What if the same consumer uses Instacart to purchase and deliver the same goods from Costco or Target? Does the consumer care which retailer the food and groceries came from when competition is just a click away? Indeed, the National Academies of Sciences concludes it is "often impossible" to distinguish between brick-and-mortar retail sales and e-commerce.[90]

E-commerce and club stores also matter for defining the geographic market. Past FTC consent orders have defined the relevant geographic markets to be areas that range from a two- to ten-mile radius around each of the merging parties' supermarkets. We conclude that, because club stores have a larger catchment area than supermarkets, it would be reasonable to expand the relevant geographic market in localities where club stores are present.

Combined, the rapid growth of e-commerce and delivery services make distance, traffic patterns, and population density decreasingly relevant in a consumer's choice of where they purchase food and groceries. Dimitropoulos and coauthors note (1) the presence of warehouse clubs expands the relevant geographic market, (2) online-delivery options expand the geographic market "far away," and (3) online food and grocery purchases can be delivered from fulfillment centers, as well as from traditional stores.[91]

Because of these observations, the product market-definition that has been employed in the FTC's consent orders over the past more than two decades is likely to be—and should be—challenged and should be revised to include warehouse clubs and to account for online retail and delivery.

IV. The Merger Is Unlikely to Increase Labor Monopsony Power

In recent years, there has been an increasing emphasis in antitrust discussions on labor markets and potential harms to workers. The recent draft merger guidelines added an explicit section on mergers that "May Substantially Lessen Competition for Workers or Other Sellers."[92] Even before the guidelines' publication, some observers predicted that the FTC was set to push a case on labor competition.[93] While, in theory, antitrust harms can occur in labor markets, just as in product markets, proving that harm is more difficult.

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[90] NATIONAL ACADEMIES OF SCIENCES, ENGINEERING, AND MEDICINE, *supra* note 7373 ("As e-commerce has grown in recent years, it has become increasingly difficult to separate out the e-commerce portion of the industry. Most e-commerce could be identified within the nonstore retailer category as of 2013, but e-commerce is becoming so pervasive that it is now not only difficult to clearly identify individual firms as predominantly e-commerce firms, but also often impossible to clearly classify individual retail sales as either e-commerce or not." *citations omitted*).

[91] Dimitropoulos, *et al.*, *supra* note 8888 ("Of course, adjustments to geographic market definition likely would need to be factored into the analysis, as club stores tend to have larger catchment areas than traditional grocery stores, and online delivery can reach as far away as can be travelled by truck from a central fulfilment center.")

[92] *Draft Merger Guidelines*, *supra* note 4, at 25-7.

[93] Maeve Sheehey & Dan Papscun, *Kroger-Albertsons Merger Tests FTC's Focus on Labor Competition,* BLOOMBERG LAW (Dec. 2, 2022) https://news.bloomberglaw.com/antitrust/kroger-albertsons-merger-tests-ftcs-focus-on-labor-competition.

An important fact about the proposed Kroger/Albertsons merger is that both companies have many unionized workers. Around two-thirds of Kroger employees[94] and a majority of Albertsons employees[95] are part of the United Food and Commercial Workers International Union (UFCW), which represents 1.3 million members. Even if the merger would increase labor monopsony power in the absence of unions, the FTC will have to acknowledge the reality of the unions' own bargaining power.

Delegates of the UFCW unanimously voted to oppose the merger[96] Rather than monopsony power or lower wages, however, the union's stated reason for their opposition was lack of transparency.[97] While lack of transparency may be problematic for the UFCW members, it does not constitute an antitrust harm. Kroger, for its part, has contended that the merger will benefit employees, citing a commitment to invest an additional $1 billion toward increased wages and expanded benefits, starting from the day the deal closes.[98] Albertsons claims that no store closures or frontline associate layoffs will result from the transaction and that the merger will "secure the long-term future of union jobs by establishing a more competitive alternative to large, non-union retailers."[99]As with most announced goals, however, there is no enforcement mechanism for this commitment at present, although one could be litigated.

Rather than relying on proclamations from any of the parties, we need economic analysis of the relevant labor markets, asking the types of questions raised above regarding the output markets. A policy report from Economic Policy Institute estimates that "workers stand to lose over $300 million annually" from the merger,[100] but the report arrives at that estimate by using an estimate of the correlation between concentration (HHI) in labor markets and wages. While academic research may benefit from such an estimate, it is unhelpful in merger analysis. As a long list of prominent antitrust economists recently wrote, "regressions of price on HHI should not be used in merger review… [A]

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[94] *Kroger Union*, UFCW (last accessed Jul. 26, 2023), https://www.ufcw.org/actions/campaign/kroger-union.

[95] *Albertsons and Safeway Union*, UFCW (last accessed Jul. 26, 2023), https://www.ufcw.org/actions/campaign/albertsons-and-safeway-union.

[96] Press Release, *America's Largest Union of Essential Grocery Workers Announces Opposition to Kroger and Albertsons Merger*, UFCW (May 5, 2023), https://www.ufcw.org/press-releases/americas-largest-union-of-essential-grocery-workers-announces-opposition-to-kroger-and-albertsons-merger.

[97] *Id.* ("Given the lack of transparency and the impact a merger between two of the largest supermarket companies could have on essential workers – and the communities and customers they serve – the UFCW stands united in its opposition to the proposed Kroger and Albertsons merger").

[98] Press Release, *Kroger and Albertsons Companies Announce Definitive Merger Agreement*, KROGER (Oct. 14, 2022), https://ir.kroger.com/CorporateProfile/press-releases/press-release/2022/Kroger-and-Albertsons-Companies-Announce-Definitive-Merger-Agreement/default.aspx.

[99] Bill Wilson, *Teamsters Union Says 'No' to Kroger, Albertsons Merger*, SUPERMARKET NEWS (Jun. 13, 2023), https://www.supermarketnews.com/retail-financial/teamsters-union-says-no-kroger-albertsons-merger.

[100] Ben Zipperer, *Kroger-Albertsons Merger Will Harm Grocery Store Worker Wages*, ECONOMIC POLICY INSTITUTE (May 1, 2023), https://www.epi.org/publication/kroger-albertsons-merger.

regression of price on the HHI does not recover a causal effect that could inform the likely competitive effects of a merger."[101]

While HHI regressions are of little practical help in this context, according to standard economic theory, it is possible that the average worker would be harmed for traditional labor-monopsony reasons. It is, however, more difficult to identify anticompetitive labor-market harms than to identify analogous product-market harms. For the product market, if the merger simply enhanced monopoly power without producing efficiency gains, the quantity sold would decrease, either because the merging parties raise prices or because quality declines. A merger that creates monopsony power will necessarily reduce the prices and quantity purchased of inputs like labor and materials. A strong union could counteract a firm's monopsony power to some extent, by collectively advocating for higher wages, fewer layoffs, and other worker benefits. Indeed, obtaining and exerting labor market power is a union's *raison d'être*.

Of course, the presence of a unionized workforce does not render monopsony impossible; unions' ability to offset the effects of a monopsony or monopoly may also be limited, and monopsony power could increase under a merger, even with unions. Still, the existence of union bargaining power makes any monopsony case more difficult and is an important factor to consider in evaluating a merger's likely labor-market effects—particularly in this case, given the high rates of union membership at both companies.

Moreover, the FTC needs to be careful with any labor case. For labor markets, a decline in the number of workers employed (which harms the workers) may not be anticompetitive. The reduction in input purchases may be *because* of efficiency gains.[102] For example, if two merging hospitals integrate their information-technology resources, therefore requiring fewer overlapping workers, the merged firm will employ fewer IT workers. This may even reduce the wages of specialized IT workers, even if the newly merged hospital does not exercise any market power to suppress wages.

The same applies for any inputs from an efficiency-enhancing merger: inputs may decrease. But using fewer inputs is not an antitrust harm. The key point is that monopsony needs to be treated differently than monopoly. The antitrust agencies cannot simply look at the quantity of inputs purchased in the monopsony case as the flip side of the quantity sold in the monopoly case, because the efficiency-enhancing merger can look like the monopsony merger in terms of the level of inputs purchased.

Another difficulty with pursuing a labor monopsony case is that the usual antitrust tools, such as merger simulation, cannot be easily applied to the labor market. Unlike the DOJ's recent success in

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[101] Nathan Miller *et al.*, *On the Misuse of Regressions of Price on the HHI in Merger Review*, 10 J. ANTITRUST ENFORCEMENT 248 (2022).

[102] *See* Geoffrey A. Manne, Dirk Auer, Brian C. Albrecht, Eric Fruits & Lazar Radić, *Comments of the International Center for Law and Economics on the DOJ-FTC Request for Information on Merger Enforcement* (2022), at 29, *available at* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4090844.

blocking Penguin-Random House from merging with Simon & Schuster on grounds that the merger would hurt authors with advances above $250,000,[103] the labor market for most employees of Kroger and Albertsons is much larger than those two companies, or even the largest definition of grocery stores. Indeed, it cannot be narrowed down to a handful of companies.

Any labor case would require showing that the merger would harm workers by reducing their bargaining power. For most workers involved, there are still many potential employers competing. One relevant piece of evidence for this is that press releases Kroger issued during the COVID-19 pandemic highlighted that the company was hiring workers from a wide variety of firms and industries—from hospitality (Marriott International) to restaurants (Waffle House) to food distribution (Sysco).[104] While we are not aware of publicly available data that would more comprehensively illustrated worker flows among different companies, such flows of retail workers into and out of roughly adjacent labor markets makes intuitive sense. As economist Kevin Murphy has explained:

> If you look at where people go when they leave a firm or where people come from when they go to the firm, often very diffuse. People go many, many different places. If you look at employer data and you ask where do people go when they leave, often you'll find no more than 5 percent of them go to any one firm, that they go all over the place. And some go in the same industry. Some go in other industries. Some change occupations. Some don't. You look at plant closings, where people go. Again, not so often a big concentration of where they go to. If you look at data on where people are hired from, you see much the same patterns. That's kind of a much more diffuse nature.[105]

If, as is likely, an overwhelming majority of Kroger's workers' next best option (what they would do if a store closed) was not an Albertsons store, but something completely outside of the market for grocery-store labor (or even outside the retail-food industry more broadly), the merger would not take away those workers' next best option. If true, the merger cannot be said to increase labor monopsony power to the extent necessary to justify blocking a merger.

V. 'Waterbed Effects' Are Highly Speculative

One potential antitrust harm that has been discussed frequently in recent years is the so-called "waterbed effect," in which "a large and powerful firm improves its own terms of supply by exercising its bargaining power, [but] the terms of its competitors can deteriorate sufficiently so as ultimately to increase average retail prices and, thereby, reduce total consumer surplus."[106] The waterbed effect

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[103] *See United States v. Bertelsmann SE & Co. KGaA*, 1:21-CV-02886, 2022 WL 16949715 (D.D.C. Nov. 15, 2022).

[104] Press Release, *The Kroger Family of Companies Provides New Career Opportunities to 100,000 Workers,* KROGER (May 14, 2020), https://ir.kroger.com/CorporateProfile/press-releases/press-release/2020/The-Kroger-Family-of-Companies-Provides-New-Career-Opportunities-to-100000-Workers/default.aspx. While the exact job-to-job switches are unknown, at least during the pandemic we know that some workers at non-grocery employers viewed at least some grocery-industry jobs as substitutes.

[105] *Transcript of Proceedings at the Public Workshop Held by the Antitrust Division of the United States Department of Justice*, U.S. JUSTICE DEPARTMENT (Sep. 23, 2019), *available at* https://www.justice.gov/atr/page/file/1209071/download.

[106] Roman Inderst & Tommaso M. Valletti, *Buyer Power and the 'Waterbed Effect'* 59 J. IND. ECON. 1, 2 (2011).

is not unique to mergers, but can apply any time there is differential buyer-market power. The firm with more market power gets a better deal from suppliers and its competitors are ostensibly harmed because they cannot get the same deal. Long before the proposed merger, but still in the context of retail, people were speculating about a waterbed effect regarding Walmart.[107]

In the context of the Kroger/Albertsons merger, critics have again raised the possibility of a waterbed effect. Michael Needler Jr.—the president and chief executive of Fresh Encounter, a chain of 98 grocery stores based in Findlay, Ohio—raised the possibility in a U.S. Senate hearing on the merger.[108] He was also quoted by *The New York Times* as saying:

> When the large power buyers demand full orders, on time and at the lowest cost, it effectively causes the water-bed effect. They push down, and the consumer packaged goods companies have no option but to supply them at their demands, leaving rural stores with higher costs and less availability to products.[109]

In a letter to the FTC, the American Antitrust Institute raised several concerns about the merger, arguing that:

> The waterbed effect is likely to worsen with Kroger-Albertsons enhanced buyer power post-merger, with adverse effects on the ability of independent grocers to compete in a tighter oligopoly of large grocery chains.[110]

The implied argument in this version of the waterbed effect goes as follows: A merged Kroger and Albertsons would have additional market power over some of its suppliers. It could then exercise that market power to extract discounts from those suppliers, which would be unavailable to its competitors. The merged firm could then pass those cost savings on to consumers in the form of lower retail prices, thereby increasing Kroger/Albertsons' sales. Some of these sales would come at the expense of smaller competitors, who could no longer compete on price. And because of these reduced sales, they would purchase less from their suppliers, further eroding their bargaining power with suppliers. Ultimately, consumers of the smaller retailers may face higher retail prices. Thus, under this theory, consumers of the merged firm would pay lower retail prices, while consumers of the smaller retailers would pay more.

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[107] Albert Foer, *Mr. Magoo Visits Wal-Mart: Finding the Right Lens for Antitrust*, AMERICAN ANTITRUST INSTITUTE WORKING PAPER NO. 06-07, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1103609.

[108] Michael Needler Jr., SENATE HEARING ON KROGER AND ALBERTSONS GROCERY STORE CHAINS, at 1:43:00, *available at* https://www.c-span.org/video/?524439-1/senate-hearing-kroger-albertsons-grocery-store-chains.

[109] Julie Creswell, *Kroger-Albertsons Merger Faces Long Road Before Approval*, NEW YORK TIMES (JAN. 23, 2023), https://www.nytimes.com/2023/01/23/business/kroger-albertsons-merger.html.

[110] Diana Moss, *The American Antitrust Institute to the Honorable Lina M. Khan*, AMERICAN ANTITRUST INSTITUTE (Feb. 7, 2023), *available at* https://www.antitrustinstitute.org/wp-content/uploads/2023/02/Kroger-Albertsons_Ltr-to-FTC_2.7.23.pdf.

Even if all of that were true, however, what remains unknown (and unaddressed under this argument) is whether consumers *as a whole* would be better or worse off. That, of course, is precisely the result that would be required to establish harm under antitrust law.

Roman Inderst & Tommaso Valletti are credited with the first formal theoretical model of a waterbed effect and how it could potentially harm consumers as a whole (as opposed to merely certain competitors or the subset of consumers who continue to buy from them).[111] In order to establish consumer harm under their model, three key assumptions must be met:

1. Retailers buy their inputs from a supplier who can price discriminate among retailers;
2. Retailers can access an alternative source of supply, but must incur a fixed switching cost, which is the same across all retailers; and
3. Retailers compete on price.

Because a larger retailer can spread the fixed switching costs across more units, its per-unit costs will be lower. This provides the larger retailer with a better bargaining position with its suppliers to extract lower input prices. If the large retailer reduces its prices to consumers, the reduced sales to smaller competing retailers results in those competitors having higher per-unit switching costs, thus reducing their ability to change suppliers, reducing their bargaining power with the initial supplier, and increasing the price they pay to the supplier for inputs.

While the model shows how the effect is possible and that it *could* harm consumers, it does not imply that the waterbed effect necessarily harms consumers. In fact, the same waterbed effect would also occur if a merger generated efficiency gains (as the authors point out), but with considerably different welfare and antitrust implications. Setting aside mergers, in Inderst & Valletti's model, if one firm discovers a cheaper importer, for example, it would give that firm more buyer power, because it presents a more credible threat of leaving for a competitor. Recognizing that the firm has a better "outside option," the wholesaler offers better terms. This, too, generates a waterbed effect, but it is clearly pro-competitive, as it would help consumers. Unless we are willing to declare finding another source of supply to be anticompetitive, we should be hesitant about jumping to the conclusion that the waterbed effect is anticompetitive.

Inderst & Valletti's model also demonstrates that, with relatively low supplier-switching costs, the supplier has little scope to price discriminate among retailers. As a result, "any further growth of the large buyer… will reduce *all* retail prices."[112] This is true even in the presence of a waterbed effect. Thus, for a waterbed effect to result in higher average retail prices for consumers, the large retailer's buying advantage must be "sufficiently larger in size," and smaller retailers must face much high

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[111] Inderst & Valletti, *supra* note 106106. For a short history of the development of the waterbed model, *see* Eric Fruits, *Sloshing Around with the "Waterbed Effect,"* TRUTH ON THE MARKET (Sep. 5, 2023), https://truthonthemarket.com/2023/09/05/sloshing-around-with-the-waterbed-effect.

[112] Inderst & Valletti, *supra* note 106106, at 9.

switching costs, with those switching costs serving as the reason why the supplier can effectively price discriminate across the retailers.[113] For many products, this simply won't be the case.

A competition authority that pursued a waterbed theory to block a merger must first demonstrate that a waterbed effect exists. Because each product sold in a food and grocery retailer may have its own idiosyncratic manufacturing, wholesale, and distribution characteristics, this evaluation likely must be conducted on a product-by-product basis. Then, for each market, the authority must evaluate the suppliers' abilities to price discriminate (which could raise additional antitrust issues). Last, the authority must evaluate competing firms' anticipated price response to any identified waterbed effect. While Inderst & Valletti provide a seemingly straightforward theoretical approach to evaluating allegations of a waterbed effect, applying their model to the real world of food and grocery mergers would likely amount to a costly and time-consuming wild goose chase.

That is likely why finding empirical demonstration of a waterbed effect has been so elusive. Indeed, we are not aware of any empirical literature indicating the existence of a waterbed effect in retail markets, let alone any evidence of consumer harms from such an effect.[114] Indeed, UK competition authorities have been unconvinced of any waterbed effects in the food and grocery mergers in which the issue has been raised. In 2006, the UK Office of Fair Trading concluded:

> [T]here are theoretical questions that would need to be resolved before concluding that the price differentials observed are evidence of a waterbed effect. For example, it is not clear how suppliers would be able to charge significantly above cost to smaller retailers without rivals undercutting them in the market; similarly, it is not clear why suppliers would price persistently below cost to the large supermarkets.[115]

In the United States, only one district court has issued an opinion on the waterbed effect. In *DeHoog*, consumers sued to block AB InBev's acquisition of SABMiller.[116] The consumers alleged that the merged firm would be a "powerful buyer" that "demands lower prices or other concessions from its suppliers, causing the supplier to, in turn, increase prices to smaller buyers." The district court rejected the consumers' waterbed claim because (1) the alleged harm was to competing brewers, not to consumers, and (2) competing brewers could switch to different hops, thereby avoiding any waterbed effect.

DeHoog highlights the high hurdles an antitrust authority or private plaintiff would need to clear in order to successfully allege a waterbed effect. Challengers must demonstrate that switching costs are

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[113] *Id.* at 10.

[114] There has been some investigation of the waterbed effect in two-sided markets in telecommunications, but these markets are very different from retail food and grocery. *See* Christos Genakos & Tommaso Valletti, *Testing the "Waterbed" Effect in Mobile Telephony*, 9 J. EUR. ECON. ASSOC. 1114 (Dec. 2011) (evaluating the effect of cutting mobile-termination fees on mobile-subscription prices).

[115] UK COMPETITION & MARKETS AUTHORITY, *supra* note 3030.

[116] *DeHoog v. Anheuser-Busch InBev*, *supra* note 3131.

insurmountably high and that a waterbed effect exists. They must demonstrate then that the waterbed effect harms consumers, rather than competitors.

Demonstrating a waterbed effect in the Kroger/Albertsons merger may be especially challenging. Although the notion has been invoked by several critics of the merger, we are not aware of any specific product or product category in which a potential waterbed effect has been alleged.[117] If the FTC chooses to pursue the waterbed-effect theory, it must identify the relevant products that would be subject to the effect and demonstrate the anticipated consumer harm associated with it. If the agency relies on the waterbed effect in an effort to block the Kroger/Albertsons merger, then it would be reasonable to conclude that its "traditional" claims of horizontal market power are especially weak.

VI. Remedies Can Resolve Any Remaining Competitive Concerns

While the above sections argue that the FTC will (and should) have a hard time making a case that the Kroger/Albertsons merger is overall anticompetitive, there may be some specific geographic markets where concerns remain. In the face of such concerns, the FTC historically has allowed most supermarket transactions to proceed with divestitures, such as Ahold/Delhaize (81 stores divested), Albertsons/Safeway (168 stores), and Price Chopper/Tops (12 stores).[118] The extent of the remedies sought depends on the extent of post-merger competition in the relevant markets, as well as the likelihood of entry by additional competitors.[119] Dimitropoulos and coauthors have noted that most divestitures required by consent orders in recent supermarket mergers have occurred in geographic markets with fewer than five remaining competitors.[120]

There is good reason (and a long history of examples in previous grocery-merger settlements) to think that targeted divestitures in certain markets—as have been proposed from the start of this process by the merging parties[121]—should be sufficient to address any geographic-market-specific concerns that may arise.

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[117] *See*, *e.g.*, Albert Foer, *Mr. Magoo Visits Wal-Mart: Finding the Right Lens for Antitrust*, American Antitrust Institute Working Paper No. 06-07 (Nov. 30, 2006), *available at* https://ssrn.com/abstract=1103609 (alleging a Walmart waterbed effect without identifying any product or product category with the relevant characteristics that would make it subject to the effect).

[118] *See In the Matter of Cerberus Institutional Partners*, *supra* note 6; *In the Matter of Koninklijke Ahold*, *id.*, *In the Matter of the Golub Corporation*, *id.*

[119] *See* Dimitropoulos, *et al.*, *supra* note 8888.

[120] *See id.*

[121] *See, e.g.,* Abigail Summerville and Anirban Sen, *Analysis: Kroger, Albertsons Spin-Off Is Extra Ammunition in Regulatory Battle*, REUTERS (Oct. 17, 2022), https://www.reuters.com/business/retail-consumer/kroger-albertsons-spin-off-is-extra-ammunition-regulatory-battle-2022-10-17 ("Kroger Co and Albertsons Cos Inc are willing to divest up to 650 supermarket stores to secure regulatory clearance for their $24.6 billion deal...."); Dan Papscun, *Kroger-Albertsons Divestiture Bid Aims to Head Off Challenge*, BLOOMBERG LAW (Oct. 14, 2022) https://news.bloomberglaw.com/antitrust/kroger-albertsons-divestiture-plan-is-bid-to-deflect-regulators ("The FTC must factor the divestiture proposal in its deal analysis, now that the companies themselves have built it into their own proposal, said Steven Cernak, a Bona Law partner. The companies' divestiture proposal makes the tie-up 'a tougher deal for the FTC to challenge,' Cernak said.").

FIGURE 3: Pre-Merger Market Overlaps Between Kroger and Albertsons

SOURCE: *Kroger*

One reason that divestiture—instead of outright blocking—should be appropriate in this case is that the vast majority of Kroger and Albertsons stores are in geographic markets where the other is not located (Figure 3). As such, there is no antitrust concerns from a product-market perspective. The merger does not affect competition in the South (where Kroger is focused) or in the Northeast (where Albertsons is focused). In these regions, the merger generates all of the efficiencies without the possible downside of a loss to competition.

In some other geographic locations, however, the companies do currently compete, and antitrust concerns could therefore arise. This is where divestiture comes in. By most measures, there appear to be some 1,400 overlapping stores; resolving this overlap entails divestiture of no more than 700, or 14% of the two companies' more than 5,000 stores.[122] By the same token, only a limited number of geographic markets have Kroger and Albertsons stores in close proximity, suggesting that targeted divestitures could address those concerns, while allowing the merger to proceed unimpeded in the great majority of markets.[123]

Previous remedies sought by the FTC in merger cases have generally been successful in achieving their goals. The FTC's most recent merger-remedies study, covering 89 orders from 2006-2012, provides additional support for the feasibility of divestitures as an effective remedy.[124] The study found that the vast majority of divestitures succeeded in maintaining competition in the affected markets.

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[122] *See Kroger/Albertsons: Companies Have Overlap of More Than 1,400 Stores; Khan Highly Critical of Failed Supermarket Divestitures*, THE CAPITOL FORUM (Nov. 2, 2022), https://thecapitolforum.com/kroger-albertsons-companies-have-overlap-of-more-than-1400-stores-khan-highly-critical-of-failed-supermarket-divestitures.

[123] *Id.*

[124] *The FTC's Merger Remedies 2006-2012: A Report of the Bureaus of Competition and Economics*, FED. TRADE COMM'N (Jan. 2017), *available at* https://www.ftc.gov/system/files/documents/reports/ftcs-merger-remedies-2006-2012-report-bureaus-competition-economics/p143100_ftc_merger_remedies_2006-2012.pdf.

All remedies involving divestiture of an ongoing business were successful. Divestitures of more limited "selected assets" also largely succeeded, although at a lower rate. Overall, the FTC concluded that more than 80% of the orders examined achieved the goal of maintaining or restoring competition post-merger.[125]

Nonetheless, despite a long history of divestitures serving as an appropriate and adequate remedy in food-retail mergers, some advocates for stronger antitrust are extremely skeptical of divestiture remedies. As authors from the American Economic Liberties Project and the Open Markets Institute put it in one recent article:

> It should not fall on our overburdened antitrust enforcers to pore over the individual assets changing hands in service of coming up with a carve-out that somehow brings a merger into technical compliance with an arbitrary Reaganite standard devised by bad-faith ideologues.[126]

Such concerns are leveled at the grocery industry, in particular, with critics consistently pointing to the Albertsons/Safeway merger divestitures to Haggen as evidence that, in this industry (if not elsewhere), divestiture is no longer an appropriate merger remedy.[127] But these arguments ring hollow. Several factors idiosyncratic to Haggen and its acquisition strategy led to that divestiture's failure.

A. Distinguishing the 2014 Haggen Divestiture

In 2014, the parent company of Albertsons announced plans to purchase rival food and grocery chain Safeway for $9.4 billion.[128] Prior to the merger, Albertsons was the fifth-largest grocer in the United States and operated approximately 1,075 supermarkets in 29 U.S. states. At the time, Safeway was the second-largest and operated more than 1,300 stores nationwide.[129] During its merger review, the FTC identified 130 local markets in Western and Midwestern states where it alleged the merger would be anticompetitive.[130] In response, Albertsons and Safeway agreed to divest 168 supermarkets in those geographic markets.[131] Haggen Holdings LLC was the largest buyer of the

[125] *Id.* at 2.

[126] Maureen Tkacik & Claire Kelloway, *The No Spin-Off Zone*, THE AMERICAN PROSPECT (Oct. 11, 2023), https://prospect.org/power/2023-10-11-no-spin-off-zone-kroger-albertsons-merger/.

[127] *See, e.g.*, Dayen, *supra* note 3 ("As the Haggen affair makes clear, the whole idea of using conditions to allow high-level mergers and competition simultaneously has been a failure."). *See also* Tkacik & Kelloway, *id.* ("The Kroger-Albertsons merger shows us why regulators need to permanently divest the concept of, well, divesting.").

[128] Scott Neuman, *Grocery Chains Safeway and Albertson's Announce Merger Deal*, THE TWO WAY (Mar. 6, 2014), https://www.npr.org/sections/thetwo-way/2014/03/06/286935900/grocery-chains-safeway-and-albertsons-announce-merger-deal.

[129] *See In the Matter of Cerberus Institutional Partners*, *supra* note 6, at 2.

[130] *See id.*, at 3-5.

[131] *See id.*, at 5.

divested stores, acquiring 146 Albertsons and Safeway stores in Arizona, California, Nevada, Oregon, and Washington.

Following the acquisition, Haggen almost immediately encountered numerous problems at the converted stores. Consumers complained of high prices, and sales plummeted at some stores. The company struggled and began selling some of its stores. Less than a year after the FTC announced the divestiture agreement, Haggen filed for bankruptcy. Following the bankruptcy, Albertsons bought back 33 of the stores it had divested in its merger with Safeway.

In retrospect, Haggen may not have been an appropriate buyer for the divested stores. Before acquiring the divested stores, Haggen was a small regional chain with only 18 stores, mostly in Washington State. The acquisition represented a tenfold increase in the number of stores the company would operate. While Haggen was once an independent, family-owned firm, at the time of the acquisition, the company was owned by a private investment firm that used a sale-leaseback scheme to finance the purchase. Christopher Wetzel notes that Haggen failed to invest sufficiently in the marketing necessary to create brand awareness in regions where Haggen had not previously operated.[132] Such issues would need to be avoided in any future divestitures, and experience shows they can be.

Around the same time that it filed for bankruptcy, Haggen also filed a lawsuit against Albertsons in federal district court, arguing that Albertsons engaged in "coordinated and systematic efforts to eliminate competition and Haggen as a viable competitor."[133] Haggen claimed that Albertsons made false representations to both Haggen and the FTC about its commitment to providing a smooth transition that would allow Haggen to be a viable competitor. Among other allegations, Haggen claimed that Albertsons overstocked the divested stores with perishable meat and produce, provided inaccurate and misleading price information that led to inflated prices, and failed to perform maintenance on stores and equipment.

None of these claims were demonstrated, as the matter settled months after the complaint was filed. Even so, FTC consent orders typically provide asset-maintenance agreements to address the kinds of issues raised by Haggen. David Balto reports that, after the 1995 Schnucks/National merger, the FTC sued Schnucks, alleging that it had violated a provision of the asset-maintenance agreement in the consent order.[134] The suit resulted in a settlement in which Schnucks paid a $3 million civil penalty and was required to divest two additional properties. These two properties were stores that had been closed by Schnucks, but that presumably could be reopened by a new buyer.

The problems with the Haggen divestiture need not be repeated. In particular, there are many companies of various sizes that have the capabilities and desire to expand. In recent merger-consent

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[132] Christopher A. Wetzel, *Strict(er) Scrutiny: The Impact of Failed Divestitures on U.S. Merger Remedies*, 64 ANTITRUST BULL. 341 (2019).

[133] Jon Talton, *Haggen: What Went Wrong?*, SEATTLE TIMES (Mar. 15, 2016), https://www.seattletimes.com/business/economy/haggen-what-went-wrong.

[134] David A. Balto, *Supermarket Merger Enforcement*, 20 J. PUB. POL'Y & MARKETING 38 (Spr. 2001).

orders, divested stores have been acquired by both retail supermarkets and wholesalers with retail outlets, including Publix, Supervalu, Big Y, Weis, Associated Wholesale Grocers, Associated Food Stores, and C&S Wholesale Grocers.[135] Several of these companies have successfully expanded—in some cases outside of their "home" territories. For example, Publix is a Florida-based chain that operates nearly 1,350 stores in seven southeastern states.[136] Publix expanded to North Carolina in 2014, Virginia in 2017, and has announced plans to expand into Kentucky this year.[137] Weis Markets is a Pennsylvania-based chain that operates more than 200 stores in seven northeastern states.[138] Last year, the company announced plans to spend more than $150 million on projects, including new retail locations and upgrades to existing facilities.[139] And Rochester, New York-based Wegmans has successfully entered Delaware, Virginia, and the District of Columbia in recent years.[140]

While the relevant product and geographic markets for supermarket mergers has shifted enormously over the past few decades, divestitures remain an appropriate and adequate remedy for any competitive concerns. The FTC has knowledge and experience with divestiture remedies and should have a good understanding of what works. In particular—and, perhaps, unlike in the Haggen example—firms acquiring divested assets should have an adequate cushion of capital, experience with the market conditions in which the stores are located, and the operational and marketing expertise to transition customers through the change.

B. Proposed C&S Divestiture

As noted, Kroger and Albertsons have contemplated divestitures from the beginning, even including a provision in their merger agreement preemptively agreeing to divest up to 650 stores.[141] More recently, however, the companies have made their divestiture plans more concrete. In September 2023, the companies presented a proposal (both publicly and to the FTC) proposing to divest 413 stores, eight distribution centers, and three store brands to C&S Wholesale Grocers for $1.9

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[135] *See In the Matter of Cerberus Institutional Partners*, *supra* note 6; *In the Matter of Koninklijke Ahold*, *id.*, *In the Matter of the Golub Corporation*, *id.*

[136] *See Facts and Figures*, PUBLIX (last visited Oct. 10, 2023), https://corporate.publix.com/about-publix/company-overview/facts-figures.

[137] *See* Caroline A., *The History of Publix: Entering New States*, THE PUBLIX CHECKOUT (Jan. 4, 2018), https://blog.publix.com/publix/the-history-of-publix-entering-new-states; Press Release, *Publix Breaks Ground on First Kentucky Store and Announces Third Location*, PUBLIX (Jun. 23, 2022), https://corporate.publix.com/newsroom/news-stories/publix-breaks-ground-on-first-kentucky-store-and-announces-third-location.

[138] Weis Markets, LINKEDIN https://www.linkedin.com/company/weis-markets/about, (last accessed Jul. 26, 2023).

[139] Sam Silverstein, *Weis Markets Unveils $150M Expansion and Upgrade Plan*, GROCERY DIVE (May 2, 2022), https://www.grocerydive.com/news/weis-markets-unveils-150m-expansion-and-upgrade-plan/623015.

[140] Russell Redman, *Wegmans lines up its next new store locations,* WINSIGHT GROCERY BUSINESS (Dec. 1, 2022) https://www.winsightgrocerybusiness.com/retailers/wegmans-lines-its-next-new-store-locations.

[141] *See, e.g.,* Summerville & Sen, *supra* note 121121.

billion.[142] The agreement also allows C&S to purchase up to 237 additional stores if needed to resolve antitrust concerns. C&S also has committed to maintain any existing collective-bargaining agreements with labor unions.[143]

The specific characteristics of the proposed buyer of the divested stores suggests that it is unlikely to fall prey to the limitations that scuttled the Haggen divestiture. Unlike Haggen, the purchasing party here has experience operating more than 160 supermarkets under brands like Grand Union. This existing operation of stores makes C&S better positioned as a buyer than Haggen was when it attempted to rapidly expand from 18 to 168 stores.[144]

While C&S is primarily a wholesaler, its Grand Union retail operations and the transition support offered under the divestiture agreement should position it to successfully operate the divested stores. In that way, the divestiture does not just spin off or increase the size of a horizontal competitor. Rather, the plan jumpstarts greater vertical integration by C&S, whose wholesale operations include the production of private-label products.

Indeed, by enabling C&S to take better advantage of the benefits of vertical integration, the divestiture appears to ensure that C&S will emerge with a structure more in line with the rest of the food-retail market. Over the past decade, many retailers (including Kroger and Albertsons) have shifted toward "bringing private label production in-house."[145] This move by firms (even without any market power) likely reflects competitive advantages gained from vertical integration.

The targeted nature of the divestiture would allow the merger to proceed in the majority of geographic markets where there are no competitive concerns between Kroger and Albertsons. Divesting stores only where localized overlaps in specific regions exist enables the realization of efficiencies and benefits in the many remaining markets. The FTC will still need to closely scrutinize the buyer and the proposed divestiture package. But the announced plan demonstrates that the merging parties are taking seriously the need for divestitures.

Of course, as with any complex business transaction, there is always some possibility that aspects of a divestiture may not fully go according to plan. The recent piece by Maureen Tkacik & Claire Kelloway throws out many of these possibilities.[146] It's *possible* that C&S turns out to not want to

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[142] *See* Catherine Douglas Moran & Petyon Giora, *Mapping Kroger and Albertson's Store Divestiture Deal with C&S*, GROCERY DIVE (Sept. 12, 2023), https://www.grocerydive.com/news/mapping-kroger-and-albertsons-store-divestiture-deal-with-cs/693186.

[143] Kroger, *supra* note 13.

[144] Grocery Dive Staff, *The Friday Checkout: C&S Would Catapult to Major Retailer Status with Kroger-Albertsons Deal*, GROCERY DIVE (Sept. 8, 2023), available at https://www.grocerydive.com/news/cs-wholesale-grocers-major-grocer-kroger-albertsons-merger-deal/693127.

[145] Catherine Douglas Moran, *Why More Grocers Are Bringing Private Label Production In-House*, GROCERY DIVE (June 13, 2023), available at https://www.grocerydive.com/news/grocers-private-label-production-in-house-sales-manufacturing/651986.

[146] Tkacik & Kelloway, *supra* note 126

run grocery stores but only wants to resell the properties. It's *possible* that C&S will be unable to afford the leases. Regulators and merging parties alike operate under inherent uncertainty when predicting competitive outcomes. Antitrust analysis does not deal with certainties, but rather with probabilistic assessments of likely competitive effects.

The relevant question is whether the divestiture is likely to effectively maintain competition in the markets of concern, not whether it can be guaranteed to perfectly do so in all scenarios. When we take more episodes than Haggen's into account, despite the uncertainty, the FTC's experience shows that targeted divestitures with an experienced buyer are likely to adequately protect consumers post-merger. The possibility that some unforeseen complication may arise does not negate the high probability that competition will be preserved. Antitrust regulation requires reasonable predictive judgments, acknowledging that business transactions inherently carry risks.

With the FTC's knowledge of the industry and of its own past successes and failures, divestitures remain an appropriate and adequate remedy for this merger. The parties appear committed to working cooperatively with regulators to craft divestitures that fully resolve competitive concerns. Rather than blocking the deal outright, the FTC can allow the merger to proceed, conditioned on acceptable divestitures that protect consumers, while permitting efficiency gains across the majority of stores.