



MCCAA

**MALTA COMPETITION AND
CONSUMER AFFAIRS AUTHORITY**

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FINDINGS OF THE OFFICE FOR COMPETITION

of 29 January 2021

**relating to proceedings under Article 9 of the Competition Act and Article 102 of the
Treaty on the Functioning of the European Union**

**Case COMP/MCCAA/12/2019 – Ex-officio Investigation regarding the Prices of Benna
Fresh Milk Products**

NON-CONFIDENTIAL

Note: Confidential information in the original version of this Decision has been redacted from the published version available on the MCCAA website. Redacted confidential information in the text of the published version of the Decision is indicated by [X].

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Executive Summary

On 23 July 2019, MDP announced that with effect from Monday 29 July 2019, it will be increasing the recommended consumer prices of Benna fresh milk products. Following this news release, the Office for Competition initiated an ex-officio investigation on the same day of the actual price increase to investigate whether the announced price increases of Benna fresh milk products are the result of an abuse of a dominant position in accordance with Article 9(2)(a) of the Competition Act and/or Article 102(a) of the Treaty on the Functioning of the European Union.

Following a thorough investigation, the Office for Competition concludes that MDP has not abused of its dominant position and therefore has not infringed Article 9(2)(a) of the Competition Act and that there are no grounds for action in relation to Article 102(a) of the Treaty on the Functioning of the European Union.

List of Abbreviations

CATI	Computer-Assisted Telephone Interviewing
EC	European Commission
ECJ	European Court of Justice
ESL	Extended Shelf Life
EU	European Union
HACCP	Hazard Analysis Critical Control Point
OFC	Office for Competition
KGS	Kilos
KPH	Koperattiva Produtturi tal-Halib Group
MCCAA	Malta Competition and Consumer Affairs Authority
MDP	Malta Dairy Products Limited
MGI	Malta Government Investments Ltd
ML	Milliliters
MMU	Milk Marketing Undertaking
MT	Malta
RCP	Recommended Consumer Price
RFI	Request for Information
ROCE	Return on Capital Employed
ROS	Return on Sales
RWP	Recommended Wholesale Price
SBS	Structural Business Statistics
SCC	Somatic Cell Count
SSNIP	Small but Significant and Non-transitory Increase in Price
TBC	Total Bacterial Count
TEC	EC Treaty
TFEU	Treaty on the Functioning of the European Union
UHT	Ultra-High Temperature processing Milk

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FINDINGS OF THE OFFICE FOR COMPETITION

of 29 January 2021

relating to proceedings under Article 9 of the Competition Act and Article 102 of the Treaty on the Functioning of the European Union

Case COMP/MCCAA/12/2019 – Ex-officio Investigation regarding the Prices of Benna Fresh Milk Products

The Office for Competition,

Having heard the submissions made by Malta Dairy Products Limited,

Having heard the submissions made by the distributors of Benna fresh milk products,

Having heard the submissions made by large retailers of Benna fresh milk products,

Having considered the provision of the Competition Act (Chapter 379 of the Laws of Malta),

Having regard to the Treaty on the Functioning of the European Union (TFEU),

Having recourse to the judgements of the Court of Justice of the European Union, and to relevant decisions and statements of the European Commission including interpretative notices on the relevant provisions of the TFEU and secondary legislation relative to competition,

Having recourse to past decisions of the Office for Competition and to those of the Competition and Consumer Appeals Tribunal and the Commission for Fair Trading,

Having regard to foreign jurisprudence,

Having given the undertaking concerned the opportunity to make known their views on the findings of the Office for Competition,

Whereas:

Section 1: Introduction

A. Background

1. The subject matter of this report was first brought to the OFC's attention by an official statement issued by MDP announcing adjustments to the recommended consumer prices of Benna fresh milk products, subsequent media articles on the subject and individual complaints during the course of the investigation.
2. On 23 July 2019, MDP announced that with effect from Monday 29 July 2019, it would be increasing the recommended consumer prices of Benna fresh milk products as follows:

Table 1: Adjustments in the Prices of Benna's Fresh Milk Products

Product	Recommended Consumer Price prior to 29/07/19	Recommended Consumer Price as from 29/07/19
Whole Milk 1L	€0.86	€0.96
Milk 2.5% fat 1L	€0.83	€0.94
Skimmed Milk 1L	€0.81	€0.92
Lactose Free Milk 1L	€1.10	€1.15
Whole Milk ½L	€0.49	€0.56
Milk 2.5% fat ½L	€0.47	€0.54
Skimmed Milk ½L	€0.46	€0.52
Lactose Free Milk ½L	€0.63	€0.65

Source: MDP's Official Statement published on 23 July 2019 titled 'Adjustments to the Prices of Benna Fresh Milk'.

3. In its statement, MDP highlighted that for the past seven years, the company managed to keep the prices of its fresh milk unchanged despite tantamount increases in the cost of feeds on the international markets as well as increases in operational costs. The company has also highlighted that the adjustments in the prices of Benna fresh milk products are limited to no more than the general rise in food prices as measured by Eurostat over the past seven years and that even at the new recommended consumer prices, its products still compete favourably when compared to fresh milk sold in other EU countries.

MDP has also announced that the higher revenue expected from the announced increases will enable the company to continue expanding its range of products on the market and to embark on a significant modernisation programme which should ensure the environmental and economic sustainability of the dairy and agricultural sectors in Malta.

4. On 29 July 2019, the OFC initiated an ex-officio investigation on the price increases of Benna fresh milk products in accordance with the provisions of Article 12(1) of the Competition Act. The scope of this report is to present the findings of the OFC's ex-officio investigation as to whether the actual price increases of Benna fresh milk products are the result of an abuse of a dominant position in accordance with Article 9(2)(a) of the Competition Act and/or Article 102(a) of the TFEU.
5. The information requested and collected by the OFC from the undertakings concerned in accordance with Article 12(2) of the Competition Act covers both Articles 5 and 9 of the Competition

Act and Articles 101 and 102 of the TFEU. Notwithstanding this, the findings of this report concern Article 9(2)(a) of the Competition Act and Article 102(a) of the TFEU.

6. This does not in any way inhibit the OFC from investigating any other alleged infringement of Articles 5 and 9 of the Competition Act and/or Articles 101 and 102 of the TFEU.

B. Overview of the Milk sector in Malta - The Local Dairy Supply Chain

7. The dairy sector is one of the most important sectors of agriculture in Malta.
8. In 2018, milk and dairy accounted for 24.3 per cent of total agricultural output which is valued at €122.1 million.¹ The Maltese dairy sector is considered to be of strategic importance:
 - a. it provides and guarantees the Maltese population and visitors with a daily supply of fresh milk products,
 - b. from an environmental perspective, it supports the use of Malta's limited arable land and agriculture. However, it is as equally important in maintaining the rural landscape and ecological character of the Maltese island.² According to statistics produced by Malta's statistics office, 5,290 hectares or 42.4 per cent of utilised agricultural arable land in the Maltese islands is used to produce forage, mainly for the dairy sector.³ The environmental benefit arising from this should not be underestimated as without the local dairy sector there would be no or very limited alternative use for the land other than urban development.
 - c. from an economic and social perspective, the dairy sector also contributes to the value added of the domestic economy by providing employment to hundreds of people – directly and indirectly – throughout the supply chain. According to statistics produced by the NSO, in 2018, the agriculture, forestry and fishing sector employed 3,430 persons, of which 2,680 persons were engaged in crop and animal production, hunting and related service activities. If one had to assume the same ratio as that for output, then it would be safe to say that almost one in every four people employed in the crop and animal production, hunting and related service activities sector is engaged within the milk and dairy sector. Jobs in this sector include production on the farms, on-farm related support services and supplies, transport, activities at the grain discharging terminal, feed mills, the dairy processing plant, milk distribution and all other support services in the milk chain.⁴ From an output perspective, it is also worth highlighting that according to the input-output tables for 2010 produced by Malta's statistics office, the output multiplier of the agricultural, forestry and fishing sector ranks in the upper half relative to the other economic sectors. Put differently, a €1 additional expenditure in the agricultural, forestry and fishing sector will have a stronger impact on the total output generated in the Maltese economy than the

¹ Source: National Statistics Office (2019), *Economic Accounts for Agriculture: 2019*. National Statistics Office News Release, 148/2019.

² P. Von Brockdorff (2002), *Development and Agri-Food Policies in the Mediterranean Region (Malta Report)*, CIHEAM Annual Report 2002, Paris: Presses de Sciences Po.

³ Source: National Statistics Office (2016), *Agriculture and Fisheries 2014*. National Statistics Office Publication.

⁴ P. Von Brockdorff and G. Buttigieg (2015), *Sectoral Impact: An Insight into How the Maltese Dairy Sector Adapted to EU Membership*, Reflection on a Decade of EU Membership, Occasional Paper 06/2015.

same additional expenditure in say, the real estate activities sector, the public administration sector or the production sector.⁵ As a result, given that the milk and dairy sector accounts for a significant share of the agricultural sector, it is safe to assume that to a certain degree, these results are reflecting the output multiplier of the milk and dairy sector.

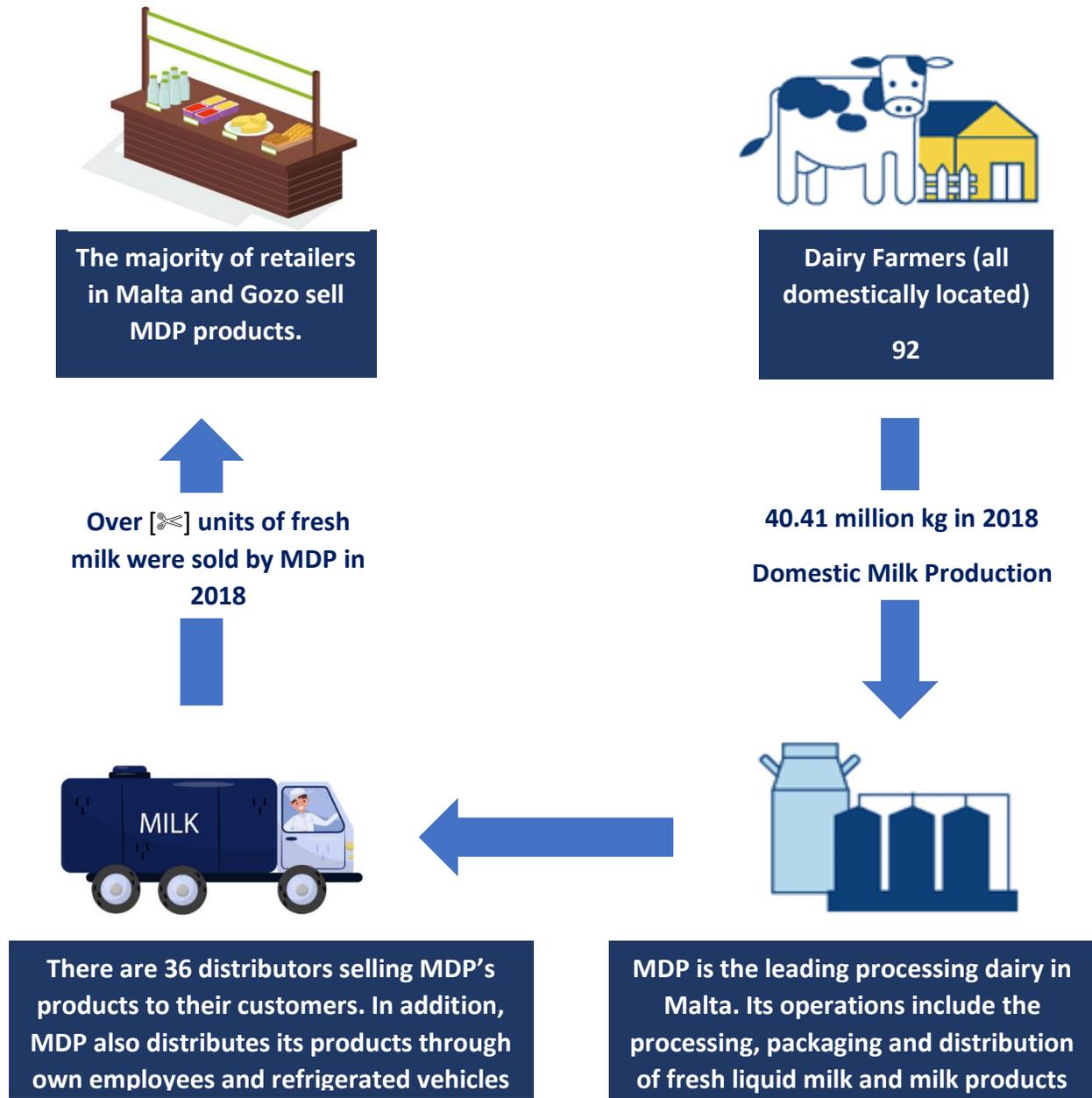
9. In 2018, the dairy sector supplied an annual production of more than 40,000 tonnes of fresh milk to the dairy processing plant. Milk produced on the island is fed to calves, used for on-farm consumption, or sold to the dairy processing plant. The dairy processing plant can then utilize milk for two purposes – fresh liquid milk for domestic consumption or manufacturing milk for yoghurts, cream, butter and a range of cheeses including mozzarella, ricotta and cheeselets. These products are then distributed to grocery retail outlets on a daily basis by a number of distributors, as presented in Figure 1. Annual retail sales of fresh milk products produced by MDP exceeded [€] in 2017 and 2018, accounting for almost [€] per cent of the total revenue generated by MDP.
10. Over the past two decades, the Maltese dairy sector had to radically adapt itself to face new challenges, the most important being Malta's accession to the EU. The sector had to adapt itself to membership, achieve a respectable degree of Europeanisation and maintain its buoyancy in the domestic market against great odds. Failure to adapt to the face of fierce competition which followed in the wake of the liberalisation of the domestic market could have easily wiped out the sector after accession, as Malta's market would have been penetrated by substitutable products from foreign producers who enjoy key advantages over Malta's counterparts, not least of these are economies of scale.
11. The Maltese dairy sector faces a number of challenges when compared to foreign counterparts:
 - a. limited arable land as well as small landholdings due to land fragmentation that results from traditional inheritance practices. According to statistics produced by the NSO, total utilised agricultural area amounted to 11,689 hectares in 2013, with arable land accounting for more than 75 per cent of the total utilised agricultural area.⁶
 - b. limited rainfall and access to water rendering virtually non-existing pastures for livestock and the production of grains and feed materials. In conjunction with the low organic content of the soil, limited rainfall also affects the quality of locally produced forage.
 - c. total reliance on imported grains and other feed materials making local dairy farmers susceptible to high sea transport costs given the comparatively small volume of purchases or imports and logistical constraints owing to Malta's geographical size and location in the periphery of Europe.
 - d. the small size of the local market makes it impossible for the dairy sector in general to benefit from economies of scales and also renders higher relative marginal costs throughout the supply chain relative to Malta's counterparts. These factors render the production of milk products of longer shelf life, such as long-life milk (UHT and/or ESL) and powder milk economically unfeasible. Such products usually serve as buffers for unsold

⁵ Source: National Statistics Office (2016), *Supply, Use and Input-Output Tables*. National Statistics Office Publication.

⁶ Source: National Statistics Office (2016), *Agriculture and Fisheries 2014*. National Statistics Office Publication.

fresh milk for many diaries across the EU. As a result, the local dairy processing plant has to maintain continuous stability between demand and supply in order to optimise the supply chain.

Figure 1: The Local Milk Supply Chain



12. Despite these limitations, the local dairy sector managed to withstand pressure from international market players and to meet several challenges that cropped up in recent years. This owes to a number of policy changes and key investment projects undertaken by the local dairy sector, some of which are listed below:

- a. EU regulations called for higher hygienic and quality standards. In order to achieve this, MDP and KPH introduced a Quality Payment Scheme whereby payment for raw milk to local dairy farmers was no longer based on the volume supplied but also on fat and protein levels. This scheme meant a considerable increase in cost to MDP but incentivised milk producers to commit themselves to improve quality and income. This improvement in raw milk hygiene and quality standards helped to improve the final quality of MDP's fresh milk products.
 - b. The successful implementation of the Quality Payment Scheme hinged on the education and training provided by KPH and MDP to local producers and the required investment towards farm upgrading and the delivery of quality raw milk to the dairy. In fact, it is estimated that the investment in farm upgrading in the dairy sector in the first ten years of EU membership totalled €40 million.⁷ Although this investment was covered by a number of schemes including the '*Modernisation of Agriculture Holdings*', '*Setting up and Use of Farm Advisory Services*' and '*Meeting Standards*' amongst others, most of the investment had to be forked out by the dairy farmers themselves.
 - c. Major investments by MDP include the upgrading of facilities at MDP's production plant with investment reaching €17.3 million by 2013, investments in expanding and diversifying its product portfolio to include a new range of milk drinks, introduction of pasteurised fresh cheeselets and new diversified range of yoghurts and desserts amongst others, an extensive rebranding exercise to strengthen and enhance the brand image of the local fresh milk products and heavy promotional campaigns and marketing.⁸
13. It is noteworthy that following EU membership, in spite of the liberalisation of imports, the removal of protective levies and harsh competition from imports, local milk production continued to increase. In fact, it is estimated that since its inception in 1986, MDP managed to achieve an annual growth of [€] per annum.⁹ Going forward, the local dairy sector will continue to face existing and new challenges, in particular; (i) the dismantling in 2015 of the quota system in milk production which used to provide market and income stability for dairy farmers and price stability for consumers, hence limiting the countervailing power of primary producers and intensifying competitive pressures from huge retail businesses across the EU, (ii) competition from EU suppliers of milk products is likely to intensify as dairies across the EU consolidate and merge, seeking increased market shares and exploiting their favourable economies of scale and lower costs of production, (iii) higher international cereal prices, pushing up costs for the local dairy sector in general, (iv) drought and desertification in Southern Europe affecting locally-grown silage to feed dairy cows besides on-farm consumption of water and (v) Malta's structural characteristics, resulting in higher costs of milk production including the opportunity cost for family labour and all the costs along the milk supply chain.

⁷ P. Von Brockdorff (2002), *Development and Agri-Food Policies in the Mediterranean Region* (Malta Report), CIHEAM Annual Report 2002, Paris: Presses de Sciences Po.

⁸ Ibid.

⁹ Source: MDP submissions.

14. These challenges call for a consolidate effort between stakeholders to work together in order to ensure that the Maltese society continues to enjoy the contribution and benefits of the Maltese dairy sector in the coming years.

C. The Local Milk Supply Chain – Market Players

15. As depicted in Figure 1, the local milk supply chain consists of four stages before reaching the end customer; milk production, milk processing and packing, logistics and the selling of fresh milk products in the grocery retail outlets.

a. Raw Milk Producers

16. The two principal stakeholders in the dairy sector are KPH, the milk producers' cooperative, and its subsidiary company MDP. KPH has been established since 1958 and today incorporates 91 dairy farmers out of the 92 producers - the non-member is the government farm located in Ghammieri.¹⁰ It is the largest farmers' organisation in terms of turnover both within the cooperative movement as well as the agriculture sector.¹¹
17. The members of KPH, the milk producers, are the owners, users and beneficiaries, and the main aim of the cooperative is to sustain and continuously improve the economic and social interests of its members, and develop the milk sector in Malta. To achieve this, over the years KPH has invested heavily and developed a vertically integrated organisation to run its core business.
18. These activities include the importation of grains and feed raw materials, the manufacture of balanced animal feed at its own feed mill, the provision of members' requirements for farm equipment, consumables and services, education and training, and technical support to its members to improve nutrition, management, efficiency, and quality. KPH also supports its members through its subsidiaries in finding a market for their production of beef and raw milk and in enhancing market competitiveness.
19. The dairy sector went through a radical upgrading and consolidation process in the first ten years of EU membership with the aim of improving efficiency, quality and competitiveness. Unsurprisingly, given the required investment and commitment, milk producer numbers supplying raw milk fell from 184 in 2003 to 120 in 2013 to 92 in 2019.¹² Evidently, not all dairy farmers could meet the financial commitment to upgrade their farms. Furthermore, a number of dairy farmers were too old to undertake the investment required, and none of their family members were interested in milk production. Others had problems in obtaining permits from the Planning Authority (formerly known as 'Malta Environment and Planning Authority' or 'MEPA') for farm restructuring and could not apply for EU funding without one. This led to the exit of a number of dairy farmers from the sector.
20. The population of dairy cows has also reported declines when compared to the pre-accession period. In 2003, the number of dairy cows stood at 7,610 compared to 6,230 in 2018. This means that between 2003 and 2018, the number of dairy cows decreased by more than 18%. Indeed, the population of dairy cows has in general experienced a downward trend over the period under consideration.

¹⁰ Source: MDP submissions.

¹¹ P. Von Brockdorff (2002), *Development and Agri-Food Policies in the Mediterranean Region* (Malta Report), CIHEAM Annual Report 2002, Paris: Presses de Sciences Po.

¹² Ibid. Figures for 2003 and 2013 were directly referenced from this paper.

21. As noted in paragraph 19, the sector also experienced a downward trend in the number of farms. In fact, as outlined in table 1 below, the number of dairy farms in 2014 stood at 120 compared to 148 in 2005. This is also mainly attributable to the reasons outlined in paragraph 13. However, it is noteworthy that when comparing 2010 to 2014, there was a shift in the farm typology by size class. These statistics highlight that while the number of dairy farms decreased by 10, the number of dairy cows increased by 140, meaning that on average the number of dairy cows per farm has increased. In fact, this could be noted from the fact that farms with a population of 100 or more dairy cows have increased from 1,725 to 2,238.

Table 2: Distribution of dairy farms and dairy cows by size class

	Size Class of Dairy Cows	1-2	3-29	30-49	50-99	≥100
	2005	Farms (148)	4	40	40	46
Number of Dairy Cows (7,675)		7	640	1,520	3,103	2,405
Size Class of Dairy Cows		1-2	3-29	30-49	50-99	≥100
2010	Farms (130)	6	45	27	39	13
	Number of Dairy Cows (6,362)	8	782	1,075	2,772	1,725
	Size Class of Dairy Cows	1-2	3-29	30-49	50-99	≥100
2014	Farms (120)	8	29	29	37	17
	Number of Dairy Cows (6,502)	12	576	1,145	2,531	2,238
	Size Class of Dairy Cows	1-2	3-29	30-49	50-99	≥100

Source: *Cattle Population: December 2005 (NSO 72/2006)*, *Cattle Census: December 2010 (NSO 031/2011)* and *Cattle Census: December 2014 (NSO 011/2015)*

22. It is also interesting to note the shift to larger dairy farms. Between 2010 and 2014, the number of dairy farms with a population size of 3-29 decreased by 16, while the number of dairy farms with a population size of 30-49 increased by 2. This is also reflected by the population of cows as in the former size, the population decreased by 206 while in the latter, the population of cows increased by 70. The same shift could be observed between the 50-99 size and the greater than or equal to 100 farm size categories. This seems to suggest that the dairy farmers who undertook the financial commitment to upgrade their dairy farms went for a bigger dairy farm.¹³

23. In spite of the challenges brought about by market liberalisation, the increase in the price of feed, the challenges to meet EU standards and regulations including the financial resources required to upgrade dairy farms, and the bolstered competition from foreign markets which factors all led to a

¹³ These reflect the author's hypothesis. In fact, this is not something which could be confirmed from existing publishable data sources.

smaller dairy cows population and a smaller number of dairy cows, milk production has remained at the levels recorded prior to EU accession.

24. In fact, according to Eurostat, raw cow's milk delivered to dairies stood at 40.02 million kg in 2003 compared to 40.41 million kg in 2018.¹⁴ This means that over the period under review, dairy farmers experienced higher yield levels relative to the herd size, as highlighted in table 3. Indeed, average cow production has increased by nearly 20 per cent between 2003 and 2018.

Table 3: Average Yearly Cow Production

2003	Number of Dairy Cows	7,675
	Raw Cow's Milk Delivered to Dairies	40.02 million kgs
	Average Cow Production in kgs	5,214
2018	Number of Dairy Cows	6,502
	Raw Cow's Milk Delivered to Dairies	40.41 million kgs
	Average Cow Production in kgs	6,215

Source: Eurostat; Author's calculations

25. Milk quality has also increased over the period under review. In fact, in 2013, TBC and SCC reached 29,000 cells/L and 280,000 cfu/ml, much better than the 100,000 cells/L and the 400,000 cfu/ml EU benchmarks. As for protein, an improvement was also registered and reached 3.22 per cent in 2013.¹⁵ Further improvements were also noted in 2018 where TBC reached 25,000 cells/L while the protein level registered marginal increases of 0.05 percentage points relative to 2013 levels.¹⁶
26. KPH holds 70 per cent shareholding of MDP and over the years, its members developed a strong and efficient supplier-buyer relationship. This ensured total quality control over the milk supply chain with KPH as the sole owner of the feed mill supplying animal feed to its members.

b. Malta Dairy Products Limited

27. MDP was set up in 1986 when it took over the operations of the then government-owned MMU. MDP is the leading processing dairy plant in Malta. MDP processes, packs and distributes fresh liquid milk and milk products originating solely from the Maltese islands. MDP's main product is fresh pasteurised milk with a range of fat content and flavours. MDP also produces a range of other products including yogurt, butter, cheese and cream. MDP employs around 120 full-time employees in both Malta and Gozo. Its main operation is located in Malta although a collection centre is also located in Gozo whose objective is to collect raw milk from Gozitan farmers in the morning and

¹⁴ Source: Eurostat statistics accessed on 8 October, 2019.

¹⁵ P. Von Brockdorff (2002), *Development and Agri-Food Policies in the Mediterranean Region* (Malta Report), CIHEAM Annual Report 2002, Paris: Presses de Sciences Po.

¹⁶ Source: MDP submissions.

send it to the main centre in Malta in the afternoon. The products supplied by MDP are distributed daily, ensuring that customers are provided with fresh milk and other dairy products.

28. The shareholding of MDP has changed over the years. The present shareholders of the company are KPH with a stakeholding of 70 per cent and the Government of Malta through MGI accounting for the remaining share.¹⁷
29. Due to the very nature of its shareholders, the Company's commitments go beyond those of other businesses. MDP is committed to supplying consumers with the best possible quality local fresh milk products in a manner which is affordable, and which promotes a feasible and sustainable supply of the necessary fresh raw milk in the Maltese territory.¹⁸
30. [REDACTED] MDP has never resorted to importing raw milk. [REDACTED] The fact that MDP produces only fresh milk products makes the matter even more complicated than it might be for other dairies and the milk sector in general within the EU.¹⁹
31. [REDACTED] In most other EU countries, when a dairy has surplus milk for its fresh milk products, it has the option to sell this surplus milk to other dairies or to produce long life products or skimmed milk powder. In Malta, the capital investment required for the production of such products is not justified for the level of use that they will be put to. As a result, matching demand and supply of milk on a daily basis is critical for the stability of the milk sector in Malta and is key in the determination of final prices of fresh milk products to the consumers, [REDACTED].²⁰
32. Furthermore, throughout the years, MDP has invested heavily in quality and efficiency and continued to improve its product portfolio in such a way as to be more competitive and in a position to meet consumers' needs and expectations. This investment, coupled with prudent pricing policy, has led to an increase in consumer demand and market growth. In fact, local milk production levels increased from a level of 31.45 million kgs in 1986 (set up of MDP) to a level of 40.41 million kgs in 2018.²¹
33. MDP has enjoyed a monopoly in the local fresh milk products sector for a considerable number of years. Up to the third quarter of 2010, there were no competitors on the local market for locally produced fresh milk products. It was only in October 2010 that a new competitor has appeared on certain products. However, this competitor did not compete with MDP's main product i.e. fresh milk which accounted for almost [REDACTED] of the total revenue generated by MDP in 2017 and 2018, respectively.²²

c. Distribution

34. [REDACTED].²³

¹⁷ Source: MDP submissions.

¹⁸ Source: MDP submissions.

¹⁹ Source: MDP submissions.

²⁰ Ibid.

²¹ Ibid.

²² Source: MDP submissions and MDP's Annual Report and Financial Statements of 2017 and 2018.

²³ Source: MDP submissions.

35. All these distributors sell the company's products to their customers, i.e. the retailers, catering establishments and other end users. In such cases, MDP has no direct relationship with these customers. It is noteworthy that these distributors are in no way exclusively bound to distribute only Benna branded products.²⁴
36. MDP also distributes itself through their own employees and own refrigerated vehicles to a number of direct customers, including retailers around Malta and Gozo. [redacted].²⁵
37. MDP issues to Distributors a price list for its products together with a RWP i.e. the recommended price at which MDP recommends that the distributor sells to its customers. MDP also includes the RCP i.e. the recommended price at which MDP recommends that its products are sold to the final consumer. The RWP is non-binding on the Distributor and the Distributor is free to sell to its customers at any price. Similarly, the RCP is non-binding on the retailer and the retailer is free to sell to its customers at any price.²⁶
38. The RCP takes into consideration the demand constraints within which MDP branded products are competitively being sold, and subject to a rational and fair allocation of value along the supply chain.²⁷

d. Grocery Retail Market

39. According to the SBS published by Eurostat, Malta had 1,061 firms operating in the retail sale of food, beverages and tobacco sector.²⁸
40. The OFC sent a request for information to a sample of grocery retail outlets. From the replies received and the research done by the OFC, the OFC is not cognizant that there are any grocery retail outlets in Malta that do not sell Benna's range of fresh milk products. This is also confirmed by MDP in their submissions.

D. Evidence gathered by the OFC following the commencement of the Investigation

41. On 23 July 2019, MDP announced that with effect from Monday 29 July 2019, it would be increasing the recommended consumer prices of Benna fresh milk products. In response to various media articles, the OFC issued a press release on the same day to clarify that in a competitive market, MDP is free to establish the pricing of its products. However, given that the OFC believes that the Benna fresh milk product range may hold a strong market position, any price increase cannot be excessive or unfair to the detriment of consumers in accordance with Article 9(2)(a) of the Competition Act and Article 102(a) of the TFEU.
42. Following first indications in the media of potential increases in Benna's milk products, the OFC had held a meeting with MDP who have been advised that should any price increase take place, the OFC will be requesting details of how the price increase was established and to this end, initiate an investigation to examine whether the actual increase in the price of milk is a result of an abuse

²⁴ Ibid.

²⁵ Ibid.

²⁶ Ibid.

²⁷ Ibid.

²⁸ Source: Eurostat statistics accessed on 8 October, 2019.

from a dominant position in breach of the Competition Act. The OFC opened a formal ex-officio investigation in accordance with the provisions of Article 12(1) of the Competition Act regarding the prices of Benna fresh milk products on 29 July 2019.

43. The OFC requested information from MDP, from the distributors and also from the retailers. This was done for four important reasons: (i) to double-check the information supplied to the OFC by each market player, (ii) to better understand how the dairy sector operates and responds at each stage of the supply chain, (iii) to investigate each market player in case of abuses arising from any possible collective dominance, and (iv) to investigate the extent to which the price increase is attributable to each player along the supply chain.
44. On 29 July 2019, the OFC requested preliminary information from MDP in accordance with the provisions of Article 12(2) of the Competition Act. The OFC requested information and/or documents from MDP on the following further occasions: meeting held with MDP on 8 August 2019, RFI sent to MDP on 8 August 2019 to which a preliminary reply was received on 2 September 2019 and the full reply received on 12 September 2019, request for clarification and pending information sent by the OFC on 30 September to which a reply was received on 14 October 2019, meeting held with MDP on 4 November 2019, and an additional RFI sent on 5 November 2019 for which a reply was received on 19 November 2019.
45. On 12 August 2019, the OFC sent an RFI to distributors who have written agreements in place with MDP to distribute Benna's range of products.
46. On 12 August 2019, the OFC sent an RFI to a sample of medium- and large-sized grocery retailers operating in Malta and Gozo. The sample consisted of twenty retail outlets. Another RFI was sent on 11 September 2020 to a sample of 12 large-sized grocery retail stores in Malta to which all the replies were received by 05 October 2020.
47. The OFC commissioned a survey on the subject which objective was to market research consumers' behaviour on the market. The primary objective of the survey was to help the OFC delineate the market definition of fresh milk and confirm whether existing case law on the subject coincides with consumers' behaviour in Malta.
48. CATI on individuals aged over 18 years residing in private households took place between the 15 and 23 of January 2020. Early terminations were not included in the final dataset to ensure consistency and limit missing data. In line with the requirements from the Data Protection Commission, the dataset was duly anonymised, and each case was given a unique code. The dataset was then checked for input errors. Fieldwork was conducted by Sagalytics.
49. Geographical region, gender and age served as the main independent variables upon which the sample is tested in terms of representativeness of the Maltese population and all of these returned high satisfactory similarity rates. The margin of error of the survey at a 95% confidence interval was of +/-4.8%.
50. Following the conclusion of the investigation, the OFC informed MDP of its intentions to publish the outcome of the ex-officio investigation in accordance with Article 30 of the MCCAA Act. To this end, pursuant to Article 29 of the MCCAA Act, the parties were requested to identify any material which they consider to be confidential, giving reasons thereof.

Section 2: Assessment - Market Definition and Dominance

A. Introduction

51. The conduct subject of this ex-officio investigation is to determine whether the actual price increases of Benna fresh milk products are the result of an abuse of a dominant position in accordance with Article 9(2)(a) of the Competition Act and Article 102(a) of the TFEU. In doing so, the OFC also examined the RWP and the RCP of the fresh milk products sold by MDP in their totality.
52. Article 9(2)(a) of the Competition Act prohibits any abuse by one or more undertakings of a dominant position within Malta or any part of Malta. In particular, it states that one or more undertakings shall be deemed to abuse of a dominant position, where it or they directly or indirectly impose an excessive or unfair purchase or selling price or other unfair trading conditions.
53. As a result, in order to establish that there has been a breach of Article 9(2)(a) of the Competition Act and/or Article 102(a) of the TFEU, the OFC must demonstrate that the undertaking/s in question: (i) holds a dominant position in the relevant market; and (ii) has abused from that dominant position.

The creation or existence of a dominant position does not breach Article 9(2)(a) of the Competition Act and/or Article 102(a) of the TFEU. Rather, it is the abuse of that position that constitutes a breach.

54. The following sections define the relevant markets and determine whether MDP or any of the market players identified in the supply chain hold a dominant position within their respective relevant market.

B. Delineating the Relevant Market

a. Legal and economic background for defining the relevant markets

55. In order to determine whether an undertaking holds a dominant position, it is first necessary to define the relevant market.²⁹ The concept of the relevant market implies the existence of effective competition between the products forming part of it, which ‘...presupposes that there is sufficient degree of interchangeability between all the products forming part of the same market in so far as a specific use of such products is concerned.’³⁰
56. Article 2 of the Competition Act defines the relevant market as “...the market for the product whether within Malta or limited to any particular area or locality within Malta, or outside Malta, and whether or not restricted to a particular period of time or season of the year”.³¹

²⁹ See for example, the judgments in *United Brands*, paragraph 10; and *Hoffmann-La Roche v Commission* C-85/76, EU:C:1979:36, paragraph 21.

³⁰ Case 85/76 *Hoffman-La Roche & Co. v Commission of the European Communities*. Judgment of the Court of 13 February 1979, paragraph 28,

³¹ Competition Act, Chapter 379 of the Laws of Malta, Article 2.

57. Market definition is a step in assessing dominance rather than an end in itself. It is a tool used to identify and define the boundaries of competition between undertakings.³² In general, the definition of the relevant market should not be an abstract exercise detached from the question of dominance.
58. Market definition typically contains two dimensions: a product and a geographic area. As is stipulated in the EC's Notice on market definition, '*...The main purpose of market definition is to identify in a systematic way the competitive constraints that the undertakings involved face. The objective of defining a market in both its product and geographic dimension is to identify those actual competitors of the undertakings involved that are capable of constraining those undertakings' behaviour and of preventing them from behaving independently of effective competitive pressure. It is from this perspective that the market definition makes it possible inter alia to calculate market shares that would convey meaningful information regarding market power for the purposes of assessing dominance or for the purposes of applying Article 85.*'³³
59. The concept of the relevant market implies that there can be effective competition between the products which form part of it. In fact, the EC's Notice on market definition states that, '*a relevant product market comprises all those products and/or services which are regarded as interchangeable or substitutable by the consumer, by reason of the products' characteristics, their prices and their intended use*'.³⁴ As such, the key question when assessing the relevant market is whether the products concerned are close enough substitutes to be sensibly regarded as being in the same market.
60. A further possible dimension to the market definition is time. An undertaking may find itself exposed to competitive constraints at one point in time but may be free from them at another.
61. The relevant product market '*is to be defined by reference to the facts in any given case, taking into account the whole economic context*'.³⁵ The economic context that may be taken into account includes, but is not limited to: (i) the objective characteristics of the products; (ii) the degree of substitutability or interchangeability between the products, having regard to their relative prices and intended use; (iii) the competitive conditions; (iv) structure of supply and demand; and (v) the attitudes of consumers and users.³⁶ The factors are not, however, fixed or exhaustive and each will depend on its own facts.³⁷
62. The process of defining a market typically begins by establishing the closest substitutes to the product that is the focus of the investigation. As is stated in the EC's Notice on market definition, based on preliminary information available or information submitted by the undertakings involved, the OFC will usually be in a position to broadly establish the possible relevant markets within which for instance, a restriction of competition has to be assessed. '*In general, and for all practical purposes when handling individual cases, the question will usually be to decide on a few alternative possible relevant markets. For instance, with respect to the product market, the issue will often be*

³² See Commission Notice on the definition of the relevant market for the purposes of Community competition law (97/C 372/03).

³³ Ibid, paragraph 2.

³⁴ Ibid, paragraph 7.

³⁵ Aberdeen Journals I, [101], cited in Case CE/9742-13 Unfair pricing in respect of the supply of phenytoin sodium capsules in the UK, December 2016.

³⁶ Ibid.

³⁷ Aberdeen Journals v Director General of Fair Trading (1005/1/1/01). Competition Appeal Tribunal, [2002] CAT 4 [2002] Comp.A.R. 167, paragraph 97.

*to establish whether product A and product B belong or do not belong to the same product market’.*³⁸

63. The process of gathering evidence on the relevant market usually involves the OFC contacting the main customers and the main companies in the industry and enquire their views about the boundaries of products and geographic markets and obtain the necessary factual evidence to reach a conclusion. The OFC might also contact the relevant professional associations, and companies active in upstream markets, so as to be able to define, in so far as necessary, separate product and geographic markets, for different levels of production or distribution of the products/services in question.³⁹
64. Where appropriate, the OFC will address written requests for information to the market players mentioned above. These requests will usually include questions relating to the perceptions of companies about reactions to hypothetical price increases and their views of the boundaries of the relevant market. They will also ask for the provision of the factual information the OFC deems necessary to reach a conclusion on the extent of the relevant market.⁴⁰ Contemporary evidence as to how the allegedly dominant undertaking itself views its competitors, and vice versa, may depending on the particular circumstances, be of decisive importance when it comes to defining the market in any given case.⁴¹
65. The EC’s Notice on market definition explicates that firms are subject to three core competitive constraints: demand substitutability, supply substitutability and potential competition. *‘From an economic point of view, for the definition of the relevant market, demand substitution constitutes the most immediate and effective disciplinary force on the suppliers of a given product, in particular in relation to their pricing decisions.’*⁴² Demand substitution constitutes customers switching some or their entire purchases from the focal product to other substitute products following a price rise. Indeed, *‘the exercise of market definition consists of identifying the effective alternative sources of supply for the customers of the undertakings involved, in terms both of products/services and of geographic location of suppliers’.*⁴³
66. In order to establish which products are close substitutes to be in the relevant market, a conceptual framework known as the hypothetical monopolist test is usually employed. The hypothetical monopolist test seeks to establish whether a hypothetical monopolist of the focal product in the geographic area in which the product is sold could profitably sustain a small but significant non-transitory increase in price. If such a price increase is profitable, then the test is complete and the focal product is the relevant market. If not, then the test is repeated by assuming that the hypothetical monopolist controls both the focal product and its closest substitute. The test is repeated until it is profitable for the hypothetical monopolist to sustain a SSNIP.⁴⁴

³⁸ Commission Notice on the definition of the relevant market for the purposes of Community competition law (97/C 372/03), paragraph 26.

³⁹ Ibid, paragraph 33.

⁴⁰ Ibid, paragraph 34.

⁴¹ *Aberdeen Journals v Director General of Fair Trading* (1005/1/1/01). Competition Appeal Tribunal, [2002] CAT 4 [2002] Comp.A.R. 167, paragraph 104.

⁴² Commission Notice on the definition of the relevant market for the purposes of Community competition law (97/C 372/03), paragraph 13.

⁴³ Ibid.

⁴⁴ Ibid, paragraphs 15-19.

67. In practice, a SSNIP is often interpreted as a price rise of 5 to 10%. However, if it is shown that a hypothetical monopolist could profitably sustain a higher price rise above the competitive level, then the test is complete and the relevant market is defined.
68. Furthermore, there are a number of quantitative tests that have been specifically designed for the purpose of delineating markets. These tests consist of various econometric and statistical approaches of price elasticities and cross-price elasticities for the demand of a product, price correlations and cointegrating relationships aimed at capturing causation relationships.⁴⁵
69. On the other hand, supply substitution occurs if undertakings are able to '*switch production to the relevant products and market them in the short-term without incurring significant additional costs or risks in response to small and permanent changes in relative prices*'. When these conditions occur, the additional production put on the market will constrain the competitive behaviour of existing production.⁴⁶
70. The third source of competition constraint is potential competition. However, potential competition is not analysed at the stage of market definition but is examined at a later stage in the context of considering barriers to entry.⁴⁷

b. Approach adopted by the OFC for defining the relevant markets

71. There is no hierarchy between different types of evidence on issues involving market definition and therefore in line with the EC's Notice on market definition⁴⁸, it is the discretion of the OFC to determine what evidence it chooses to rely on to establish a relevant market.
72. As highlighted in paragraph 63, evidence of how an undertaking sees the market is likely to be '*particularly significant*' and depending on the particular circumstances, it may be of '*decisive importance*'.⁴⁹
73. In delineating the relevant market, the OFC relied on three important sources of information. These are: (i) requests for information to the market players asking their views on the boundaries of the relevant market, (ii) evidence from recent local and foreign case law and market studies on the subject that offer actual examples of product and geographic substitutability including the views of competitors, and (iii) survey aimed at eliciting the views and preferences of customers on the boundaries of the product market as well as counterfactuals relating to the SSNIP test. The latter source is also used to produce information on the barriers and costs associated with switching demand to potential substitutes.
74. The following section aims to discuss and present the information derived from each source on an individual basis.

⁴⁵ Ibid, paragraph 39.

⁴⁶ Ibid, paragraph 20.

⁴⁷ Ibid, paragraph 24.

⁴⁸ Ibid Paragraph 25.

⁴⁹ Aberdeen Journals v Director General of Fair Trading (1005/1/1/01). Competition Appeal Tribunal, [2002] CAT 4 [2002] Comp.A.R. 167, paragraphs 103 and 104.

c. The Relevant Product Market

75. For the purpose of this investigation, the focal product is the below selection of Benna's fresh milk products (the 'Focal Product'):

- a. Fresh Whole Milk 3.5% fat (500ml and 1000ml)
- b. Fresh Milk 2.5% fat (500ml and 1000ml)
- c. Fresh Skimmed Milk 0.3% fat (500ml and 1000ml)
- d. Fresh Lactose Free Milk 2.5% fat (500ml and 1000ml)

Given that the price increases announced by MDP on 23 July 2019 concern the above range of fresh milk products, the scope of this investigation is solely on the above.

76. For the purposes of this investigation, the focal product is the same for MDP, for the distributors engaged with MDP and for the grocery retail sector. However, for raw milk producers, the focal product is assumed to be raw milk.

77. As identified in paragraph 74, fresh milk comes in several forms including full-fat, low-fat, skimmed and modified.⁵⁰ On the other hand, raw milk '*refers to any type of milk that hasn't been treated through a process like pasteurisation*'.⁵¹

78. In order to properly delineate the market for fresh milk products, the OFC identified the following types of milk as the most likely substitutes for the Focal Product:

- a. Concentrated Milk; '*concentrated milk is made by removing moisture from milk. Condensed milk is one form of concentrated milk, made by increasing milk solids to 28%, canning and then sterilising it. Sweetener is sometimes added.*

*Powdered milk is another form of concentrated milk. This is made through a similar process with a milk concentrate made up of about 40% milk solids, which is then dried to reduce moisture to just 3%.*⁵²

- b. Long-life milk; '*this milk is superheated so that all microorganisms and heat-resistant enzymes are deactivated. For example, regular fresh milk is heated to 74°C for 15 seconds, while long-life milk (otherwise known as Ultra-Heat Treatment or UHT) is heated to 140°C for two seconds*'.⁵³
- c. A1/A2 milk; '*A1 and A2 refer to a specific protein found in milk called beta casein. Different breeds of cows produce milk with more or less of either A1 or A2 protein*'.⁵⁴

⁵⁰ The OFC is cognizant that MDP also produces flavoured fresh milk. However, since the price of flavoured fresh milk remained the same as it was pre 29 July 2019, flavoured fresh milk falls outside the scope of this investigation and is therefore not subject to the OFC's investigation.

⁵¹ Dairy Australia's website, accessed 23 October 2019, < <https://www.dairy.com.au/products/milk> >

⁵² Ibid.

⁵³ Ibid.

⁵⁴ Ibid.

79. In its assessment to delineate the relevant market, the OFC relied on three important sources of information as outlined in paragraph 72, which are discussed in a separate manner below.
80. In its assessment, the OFC assesses the evidence which is relevant for the assessment of market definition generally rather than considering each level of the supply chain separately. The implications of this evidence are similar regardless of the level of the supply chain being considered with the exception of raw milk producers. As a result, where it is appropriate to distinguish between different levels of the supply chain, this is clearly indicated.
81. Provided that the focal product is fresh milk, the rest of this section will focus on the focal product and will assume that for raw milk producers, the relevant market is strictly limited to cow's raw milk.

i. Information on the Relevant Market for Fresh Milk received from MDP

82. In general, evidence as to how the undertaking/s in question themselves see the market is likely to be particularly significant. *'The idea of a market is familiar. Annual reports, business plans and other documents often refer to the market in which the undertaking operates. This will normally include other undertakings which the undertaking views as its competitors.'*⁵⁵
83. Taking the above into account, the OFC requested MDP to outline whether they view other types of milk as substitutes to Benna's fresh milk and if in the affirmative, to list the main competitors of Benna's fresh milk products.
84. In their submissions, it was also noted that *'Ultra-Heat Treated (UHT) milk and Extended Shelf Life (ESL) milk all directly compete with Benna fresh milk. They are 100% substitutes of fresh milk since they are used exactly for the same purpose/s as fresh milk, namely for drinking, as a tea-coffee mixer, mixed with cereals, and used in recipes, catering and cooking.'*⁵⁶
85. As a result, it is the understanding of the OFC that MDP views fresh milk and long-life milk (ESL and UHT) as being part of the same product market and thus considers the latter to be a direct substitute to the former.
86. MDP also noted that *'Dairy free drinks such as soya drinks and almond milk also compete with fresh milk and are substitutes for some of the usages of fresh milk, for the same purposes just indicated.'*⁵⁷
87. Furthermore, it was also noted that: *'Condensed milk and powdered milk also compete with fresh milk and are substitutes for some of the usages of fresh milk (notably as a tea-coffee mixer and for cooking).'*⁵⁸
88. As a result, MDP notes that: *'...it is clear that MDP is one of numerous competitors in the domestic market for milk products, which also includes milk products with a longer shelf life (referred to as*

⁵⁵ Aberdeen Journals v Director General of Fair Trading (1005/1/1/01). Competition Appeal Tribunal, [2002] CAT 4 [2002] Comp.A.R. 167, paragraph 103.

⁵⁶ Source: MDP submissions, dated 12 September 2019.

⁵⁷ Ibid.

⁵⁸ Ibid.

*Extended Shelf Life products) as well as long-life milk products. There is a strong degree of substitutability between these products.*⁵⁹

ii. The Relevant Market for Fresh Milk – Evidence from Case Law and Market Studies

89. An important source of information which the OFC resorts to when delineating the relevant market is literature and EU and foreign jurisprudence on the subject.
90. In Friesland Foods/Campina⁶⁰, the EC concluded that there exists a separate relevant product market for long-life milk. In fact, it was noted that *“the market investigation confirmed the distinction between fresh and long-life dairy products. It revealed that despite improvements in the taste for long-life basic dairy products, customers still perceive long-life basic dairy products as different from fresh basic dairy products because of taste, shelf-life, storage possibilities and placement in the supermarket.”*⁶¹
91. As in Friesland Foods/Campina, the EC made the same distinction between fresh milk and long-life milk in Arla Foods/Milk Link both for flavoured and unflavored milk products.⁶² In its assessment, the EC noted that fresh milk and long-life milk differ in their timeline of perishability. In fact, it was noted that long-life milk *“can be kept for approximately six months at room temperature.”*⁶³ The same conclusions were also highlighted in Arla Foods/Allgäuland⁶⁴, in Arla/Hansa⁶⁵ and in Arla Foods/Express Diaries⁶⁶.
92. Furthermore, in Friesland Foods/Campina, the EC also concluded that conventional and organic milk and fresh milk constitute separate product markets.⁶⁷
93. In Tetra Pak II, the EC also felt the need to make a distinction between fresh milk and long-life milk. In fact, it was noted that even at the processing stage, there are distinctive differences as fresh milk is usually pasteurised whereas long-life milk is sterilised. Sterilisation is achieved by briefly heating the milk to an ultra-high temperature (UHT) under aseptic conditions. This process prolongs the expiration time of the milk and also allows for it to be stored in a non-refrigerated environment.⁶⁸
94. Furthermore, it was also noted that there are salient differences when it comes to packaging. UHT-milk cannot be packaged in the same type of cartons as fresh milk, since UHT-milk, once sterilised, must remain in a sterile environment until opened and consumed. Consequently, milk can be packaged by two methods: non-aseptic for fresh milk and aseptic for UHT milk.
95. In its previous assessment, the OFC has also considered the market for fresh milk products to be separate from that of long-life milk products. In fact, it was noted that:

⁵⁹ Ibid.

⁶⁰ COMP/M.5046 – Friesland Foods/Campina, published on 17/12/2008.

⁶¹ Ibid, paragraph 139.

⁶² COMP/M.6611 – Arla Foods / Milk Link, published on 27/09/2012.

⁶³ Ibid, paragraph 26.

⁶⁴ Case COMP/M.6348 – Arla Foods/Allgäuland, paragraph 23.

⁶⁵ COMP/M.6119 – Arla/Hansa, paragraph 23.

⁶⁶ COMP/M.3130 – Arla Foods/Express Diaries, paragraph 22.

⁶⁷ COMP/M.5046 – Friesland Foods/Campina, paragraph 14.

⁶⁸ 92/163/EEC: Commission Decision of 24 July 1991 relating to a proceeding pursuant to Article 86 of the EEC Treaty (IV/31043 - Tetra Pak II), paragraph 8.

“...fresh milk and long-life milk products have different characteristics. UHT treated milk tastes different from fresh milk as the former sweetens the flavour of milk by burning some of its sugars. Moreover, UHT milk has a different constitution from fresh milk as the former has an addition of antioxidants and preservatives. In addition, there are also differences in the displaying and handling of the different two types of milk. Fresh milk has a much shorter life than UHT milk as producers use a different process to preserve the latter type of milk. Given this difference, fresh milk is refrigerated while long-life milk is displayed on supermarket shelves. Moreover, there are also differences in the distribution of these two types of milk. Long-life milk is distributed on ambient lorries while fresh milk must be refrigerated at all times and distributed within a constrained time frame.

Fresh and long-life milk are also distinguished on the supply side perspective. The production methods of the two types of milk differ in terms of processes and plant. In fact, a processor of fresh milk cannot shift its production to long-life milk and market it in the short term without incurring significant additional costs. This is due to the fact that production of long-life milk requires additional machinery to produce.”⁶⁹

96. In Lactalis/Parmalat⁷⁰, the EC has also considered a further sub-segmentation according to species (cow, goat and sheep). However, since MDP only resorts to raw milk produced by cows for manufacturing its fresh milk products, the OFC did not feel the need to further sub-divide the market according to species.

iii. Results of the Demand-Side Survey

97. Approximately three out of every four respondents interviewed do not consider long-life or condensed milk as a substitute for fresh milk. Quality, freshness, health, nutrition, duration of the product, product availability and intended use have been noted as the most important attributes when choosing milk.
98. Nearly 60% of the respondents prefer not to buy any milk if fresh milk is not available despite having four out of every five respondents who have consumed long-life and/or condensed milk and nearly two out of every three respondents interviewed who are willing to consume long-life and /or condensed milk. A high proportion of respondents recognised a number of characteristics which are different between fresh milk and long-life and condensed milk including taste, health, nutrition and duration of the product.
99. According to this survey, price is not considered to be the most important factor when choosing milk. In fact, nine out of every ten respondents surveyed have disagreed with the statement that long-life and/or condensed milk is not consumed because it is more expensive than fresh milk. When presented with a number of counterfactuals, only a maximum of two out of every ten respondents interviewed were willing to either switch to foreign fresh milk products or switch to condensed and/or long-life milk in response to a hypothetical increase in the price of fresh milk of 20%. Indeed, nearly all respondents have continued to consume the local fresh milk product following the price increases announced by MDP on 23 July 2019. While this reflects a strong degree of brand loyalty towards the local fresh milk product, it is noteworthy that the Benna range of fresh milk products remains one of the cheapest options for consumers when it comes to milk consumption even when considering long-life and/or condensed milk.

⁶⁹ COMP/CCD/7/11 – Alleged infringement by Malta Dairy Products Limited of Article 9 of the Competition Act with regards to the excessive pricing of milk products, page 9.

⁷⁰ COMP/M.6242 – Lactalis/Parmalat, paragraph 9.

100. Box A presents the full results of the survey conducted with the demand-side of the market.

Box A: Eliciting Consumer Behaviour on the Market of Dairy Milk – The Case of Malta

Survey Results – Key Insights

Survey Instrument and Sample

Data for eliciting consumer behaviour and perceptions of fresh milk in the Maltese grocery retail market was collected by means of a population-based survey (Appendix A). Besides basic socio-demographic data, the survey included three sections. The questions included in the first section are aimed to assist the OFC in defining the relevant market. The second section aims to analyse the extent of demand-side substitutability between fresh milk and long-life and condensed milk while the last section presents a number of counterfactuals and records respondents' answers in each scenario.

Computer-assisted telephone interviewing (CATI) on individuals aged over 18 years residing in private households took place between the 15 and 23 of January 2020. Early terminations were not included in the final dataset to ensure consistency and limit missing data. In line with requirements from the Data Protection Commission, the dataset was duly anonymised, and each case was given a unique code. The dataset was then checked for input errors. Fieldwork was conducted by Sagalytics.

The sample data consists of 411 respondents collected from amongst the Maltese population. Geographical region, gender and age serve as the main independent variables upon which the sample is tested in terms of representativeness of the Maltese population and all of these return high satisfactory similarity rates as illustrated in tables 1-3.

Table 4: Statistical significance by Geographical Region at a 95% confidence interval

	Geographical Region (n=411)		
	Population (%)	Sample (%)	Difference (in pp.)
Southern Harbour	19	19	0
Northern Harbour	28	25	3
Southern Eastern	15	16	-1
Western	15	15	0
Northern	15	15	0
Gozo and Comino	7	10	-2

Table 5: Statistical significance by Gender at a 95% confidence interval

	Gender (n=411)		
	Population (%)	Sample (%)	Difference (in pp.)
Male	49	49	0
Female	51	51	0

Table 6: Statistical significance by Age Group at a 95% confidence interval

	Age Group (n=411)		
	Population (%)	Sample (%)	Difference (in pp.)
18-25	11	12	-1
26-35	19	17	2
36-45	16	14	2
46-55	14	17	-3
56-65	17	20	-2
66+	23	21	2

The above tables provide the percentages of the population demographics and of the sample. The last column in each table includes a 'Difference' percentage which is the difference between the population percentage and the sample percentage. It is clear from the above that the differences are within the margin of error of this study i.e. +/-4.8%. Hence, the sample is representative of the Maltese population.

Findings

I. Who are the Respondents? – Key Characteristics

- a. **Number of People living in Household:** 8.5% of the respondents are single individual households while 24.1% and 18.5% of the respondents live in households composed of three and four adults, respectively. 70.1% of the respondents do not have children aged under 16 years of age, while 19.2% have one child under 16 years of age. 9.5% of our respondents have two dependent children.
- b. **Gender:** 48.7% of respondents are males, while 50.6% are females. 0.7% of respondents preferred not to answer.
- c. **Age:** More than one-fifth of the respondents reported their age to be equal to or greater than 66 years old. Nearly 20% reported their age to fall in the 56-65 years age bracket, while 14.3% reported their age to be within the 36-45 years age bracket. 11.9% reported their age to fall in the 18-25 age bracket while the remaining respondents are evenly split between the 26-35 and 46-55 age brackets. These percentages are broadly in line with the demographic statistics published by the National Statistics Office and are therefore regarded to be a good representation of the Maltese economy.
- d. **Region of Residence:** Nearly one-fourth of the respondents live in the Northern Harbour region in line with the NSO Demographic Review 2014. Nearly 20% of the respondents live in the Southern Harbour region (NSO Demographic Review 2014 – 18.6%) while 16.3% live in the South Eastern region (15.6%). 15.3% (15.4%) and 14.8% (13.8%) of the respondents live in the Northern region and Western region, respectively, while 9.5% (7.4%) of the respondents live in Gozo and Comino.
- e. **Education:** Approximately 40% of the respondents reported secondary education as their highest level of education, while nearly 30% of the respondents reported a tertiary or higher level of education. 18.5% of the respondents reported that their highest level of education is post-secondary, while 10.7% of the respondents noted that they have a primary level of education as their highest level of education.

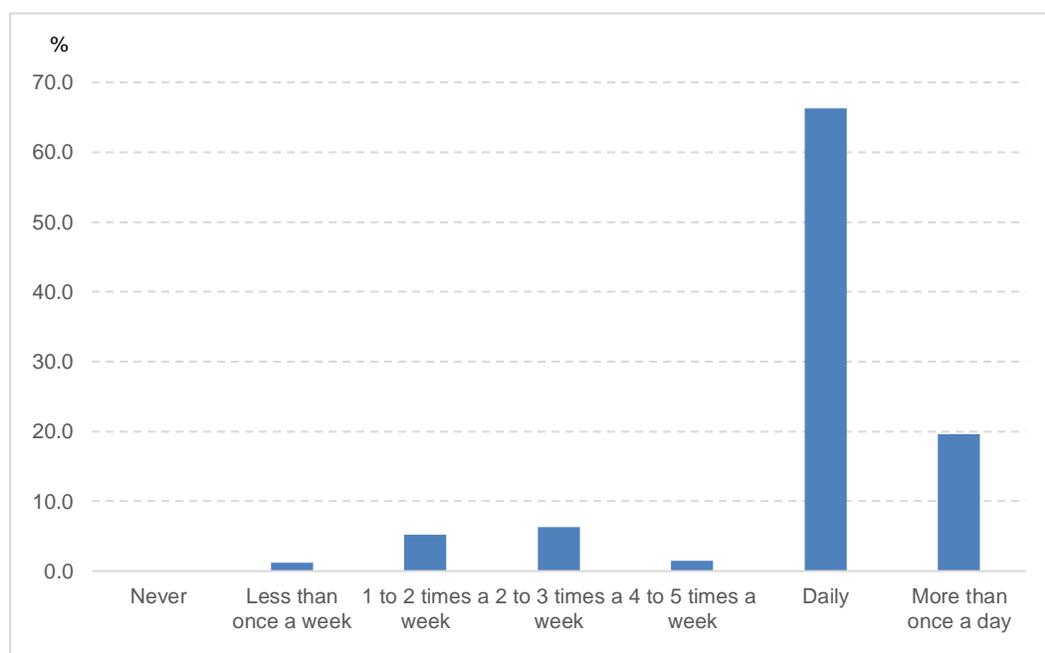
- f. **Labour Status:** More than half of the respondents are employed while 42.3% of the respondents are inactive of which 20.4% are retired while 17.8% reported that they are domestic engineers. This composition compares well with the statistics produced by NSO in the Labour Force Survey 2020/Q1.

II. Defining the Relevant Market – Key Insights

This section analyses whether from the demand-side, fresh milk constitutes a separate product market from the market of long-life and condensed milk. Particular attention is being devoted to this topic since the market for fresh milk in Malta is highly concentrated, and the conclusion that fresh milk constitutes a separate product market means that the fresh milk products of Malta Dairy Products Limited have very limited substitutes on the local market. As a result, such a conclusion highly affects the dominance position of Malta Dairy Products Ltd. Given its importance, the Office followed the guidelines of the European Commission and gathered primary data on the market at hand. It is noteworthy that these questions were only answered by those respondents who have themselves or anyone within their household consumed unflavoured liquid milk.

- a. **You or anyone in your household consumed unflavoured liquid milk:** 84.4% (or 347 respondents) of the respondents responded affirmatively while the rest (64 respondents) did not consume any unflavoured liquid milk.
- b. **Frequency of unflavoured liquid milk consumption:** Nearly two-thirds of the respondents answered that themselves or anyone within their household consumed milk on a daily basis. 19.6% of the respondents highlighted that they consume milk more than once a day while 11.5% of the respondents noted that they consume milk 1 to 2 times a week and 2 to 3 times a week, broadly equally split between these categories. The results are depicted in Figure 2.

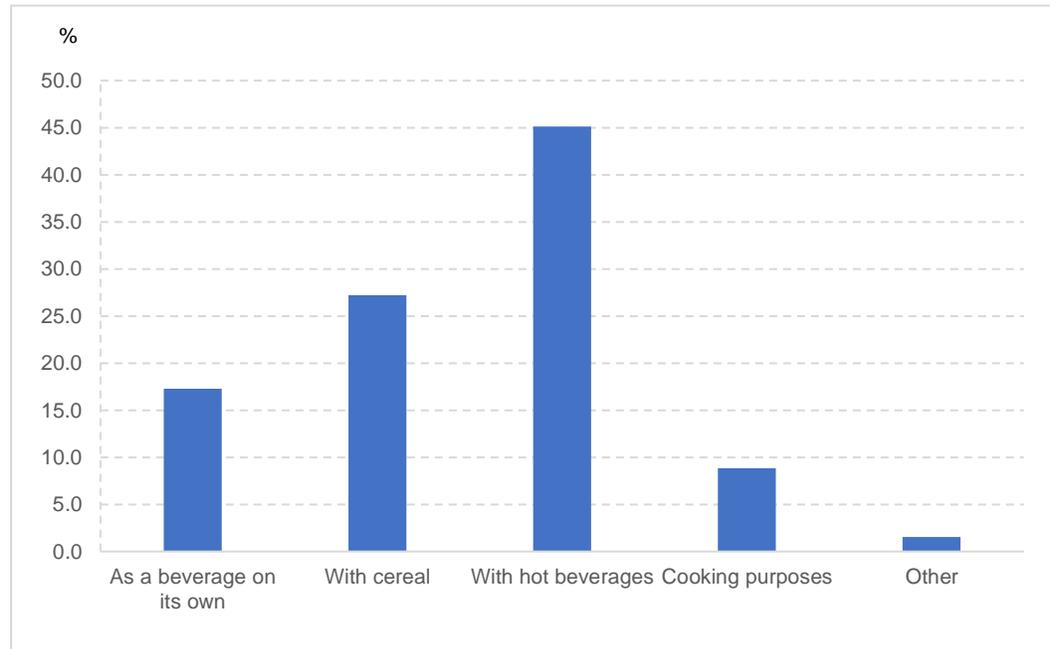
Figure 2: How often did you or anyone in your household consumed milk?



- c. **Purpose for unflavoured milk consumption:** The majority of respondents consume milk with hot beverages while 27.2% of the respondents consume milk with cereal. 17.3% of the respondents consume milk as a beverage on its own, while 8.9% of the respondents noted

that they consume milk for cooking purposes. The rest noted that they consume milk for other reasons, with milkshakes and infant milk being the most popular. The results are depicted in Figure 3.

Figure 3: For what purpose, did you or anyone in your household consumed milk?



- d. **Type of milk consumed:** More than three-fourths of the respondents answered that themselves or anyone within their household consumes fresh milk. On the other hand, 20.8% of the respondents answered that they consume long-life milk, while less than 5% of the respondents noted that they consume concentrated milk. More than 98% of the respondents highlighted that they consume the local Benna fresh milk product.
- e. **Type of fresh milk consumed:** Nearly [] of the respondents consume fresh skimmed milk, while [] of the respondents consume fresh whole milk. [] of the respondents consume fresh milk 2.5% fat while [] consume fresh lactose free milk 2.5% fat. Flavoured milk is the least popular, gaining a score of []. The results are depicted in Figure 4.

Figure 4: What type of fresh milk do you or anyone in your household usually consume? [8]



- f. **Size and Price of fresh milk:** 86.4% of the respondents buy fresh milk in 1 litre cartons while 12.3% of the respondents buy fresh milk in half-litre cartons. 1.3% of the respondents noted that they buy both sizes regularly.

When asked whether respondents are aware of the prices of the 500ml and the 1L fresh local produce milk carton, for the former size, 10.4% of the respondents answered that they know while for the latter, 27.8% responded affirmatively.

Figure 5: Consumer Awareness and Perception of the Price of a 500ml Fresh Locally Produced Milk Carton

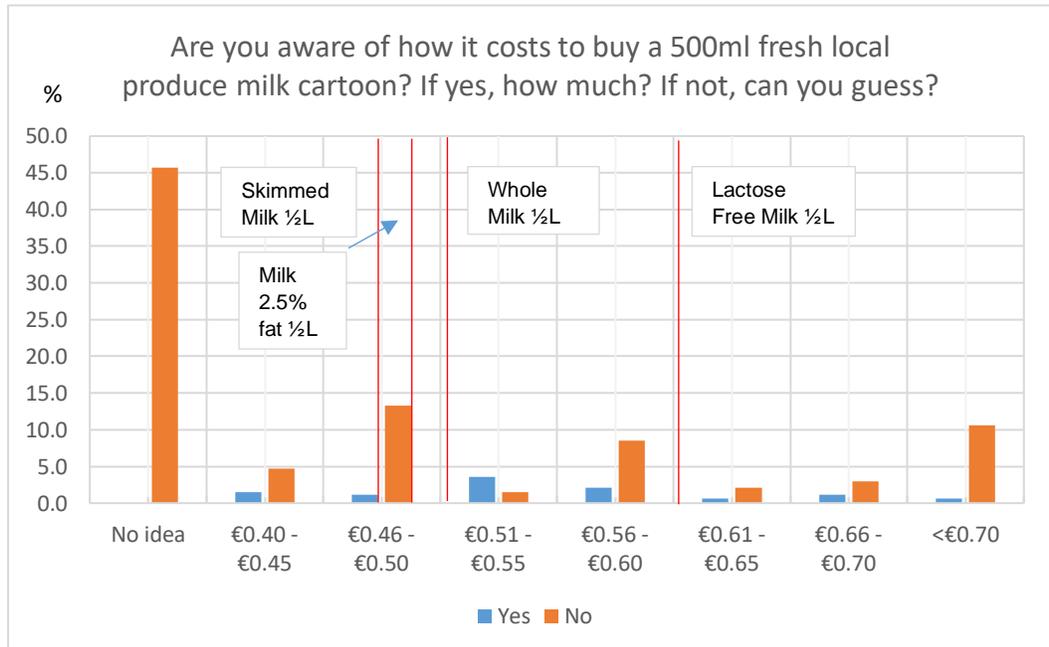


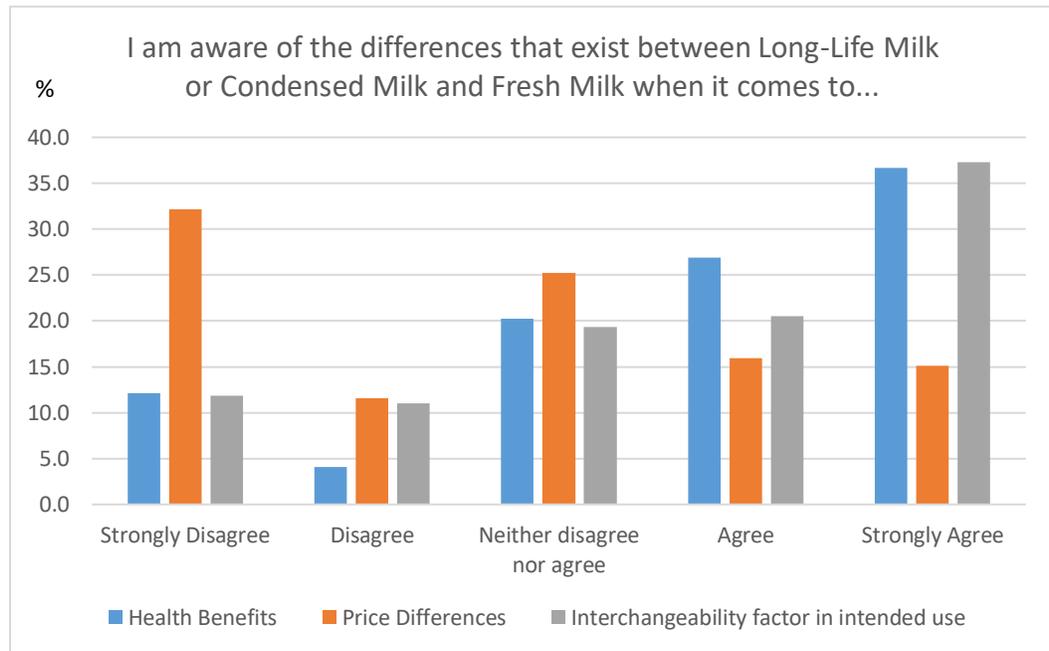
Figure 6: Consumer Awareness and Perception of the Price of a 1000ml Fresh Locally Produced Milk Carton



Nearly half of the respondents answered that they do not know the price and neither have an indication of the price of a 500ml fresh locally produced milk carton compared to nearly 20% for the 1000ml carton size. In fact, it turned out that the majority of respondents are information asymmetric on the price of locally produced fresh milk. Out of those that indicated that they are informed on the price of locally produced fresh milk, the majority quoted a price which is in the region of the price of the most popular products of fresh milk. Figures 5 and 6 depict the results of the 500ml carton size and the 1000ml carton size, respectively.

- g. **Information Asymmetry:** 63.6% of the respondents either 'Strongly Agree' or 'Agree' when it comes to awareness on the health differences that exist between Long-Life Milk or Condensed Milk and Fresh Milk compared to 57.8% scored for the interchangeability factor in the intended use. In line with what was observed in Figures 5 and 6, only 31% of the respondents 'Strongly Agree' or 'Agree' when it comes to price differences between Long-Life Milk or Condensed Milk and Fresh Milk. At the same time, a higher proportion of respondents (43.8%) are information asymmetric when it comes to price differences between Long-Life Milk or Condensed Milk and Fresh Milk compared to the scores of the interchangeability factor in intended use (22.8%) and health benefits (16.2%). Figures 7 illustrates the results.

Figure 7: Awareness of the Health Benefits/Price Differences/Interchangeability factor in intended use that exist between Long-Life Milk or Condensed Milk and Fresh Milk



III. Demand-Side Substitutability between Fresh Milk and Long-life or Condensed Milk

- a. **The extent of demand-side substitutability between Long-Life or Condensed Milk and Fresh Milk:** Nearly three-fourths of the respondents do not consider long-life milk or condensed milk as a potential substitute for fresh milk.

More than 30% of the respondents noted that their reason for considering or for not considering long-life milk or condensed milk as a potential substitute to fresh milk is attributed to taste reasons. 28.7% of the respondents noted that this is due to health reasons while the convenience and nutritional elements each achieved a score of more than 12%. The least popular reason is price, achieving a popularity of less than 1%. Figure 8 depicts the results.

- b. **Important Attributes when choosing milk:** More than 90% of the respondents have declared that quality, freshness and duration of the product are 'Important' and 'Very Important' when choosing milk. High scores close to 90% have also been recorded for health, nutrition, availability and intended use. As was the case in the previous survey questions, the price factor scored relatively low, with only 41.6% of the respondents declaring it to be an important attribute. This is coupled with a relatively higher percentage of respondents declaring it unimportant. Less than 5% of the respondents have declared the other attributes other than price to be either 'Least Important' or 'Not Important'. Table 7 illustrates the results.

Figure 8: Demand-side substitutability between Long-Life Milk or Condensed Milk and Fresh Milk [✂]

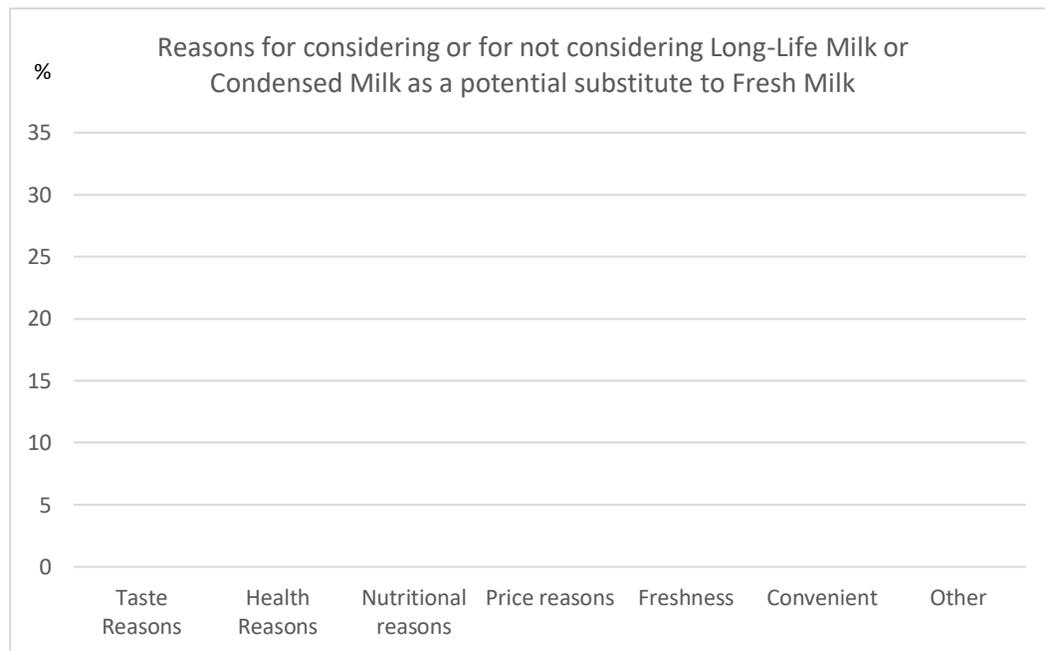


Table 7: To what extent do you assign importance to each of these attributes when choosing milk?

%	Least Important (1)	Not Important (2)	Neutral (3)	Important (4)	Very Important (5)
Price	[✂]	[✂]	[✂]	[✂]	[✂]
Quality	[✂]	[✂]	[✂]	[✂]	[✂]
Freshness	[✂]	[✂]	[✂]	[✂]	[✂]
Availability	[✂]	[✂]	[✂]	[✂]	[✂]
Duration of Product	[✂]	[✂]	[✂]	[✂]	[✂]
Nutrition	[✂]	[✂]	[✂]	[✂]	[✂]
Health	[✂]	[✂]	[✂]	[✂]	[✂]
Intended Use	[✂]	[✂]	[✂]	[✂]	[✂]

- c. **Key Insights on Consumer Behaviour in the Market of Milk:** While nearly 80% of the respondents have consumed long-life and/or condensed milk and 65.7% responded that they are willing to consume long-life and/or condensed milk, 56.4% of the respondents prefer not to buy any milk if fresh milk is available. Furthermore, 92.2% of the respondents highlighted that there are taste differences between long-life and/or condensed milk when compared to fresh milk while more than 85% of the respondents answered that they prefer fresh milk as opposed to long-life and/or condensed milk due to the health benefits of the former relative to the latter. When it comes to the long-lasting aspect, long-life and/or condensed milk scored relatively low when compared to fresh milk while more than half of the respondents highlighted that they only use long-life and/or condensed milk when fresh milk is not available. Again, the price element attained low scores as 92.8% of the respondents have responded that the price element is not

considered to be an important factor when choosing between long-life or condensed milk and fresh milk. The results are illustrated in table 8.

Table 8: To what extent do you agree with the following statements?

%	Strongly Disagree (1)	Disagree (2)	Neither disagree nor agree (3)	Agree (4)	Strongly Agree (5)
I prefer not to buy any milk if Fresh Milk is not available	[✂]	[✂]	[✂]	[✂]	[✂]
I only use Long-Life/Condensed Milk when Fresh Milk is not available	[✂]	[✂]	[✂]	[✂]	[✂]
I prefer to consume Long-Life/Condensed Milk because it is more convenient and saves me shopping time (long-lasting)	[✂]	[✂]	[✂]	[✂]	[✂]
In my opinion, Fresh Milk and Long-Life/Condensed Milk have the same taste	[✂]	[✂]	[✂]	[✂]	[✂]
I do not consume Long-Life/Condensed Milk because it is more expensive than Fresh Milk	[✂]	[✂]	[✂]	[✂]	[✂]
I prefer Fresh Milk because I perceive it as healthier than Long-Life/Condensed Milk	[✂]	[✂]	[✂]	[✂]	[✂]
Consumers have a wide variety of Fresh Milk to choose from	[✂]	[✂]	[✂]	[✂]	[✂]
Up to now I have never consumed Long-Life/Condensed Milk	[✂]	[✂]	[✂]	[✂]	[✂]
I am not willing to consume Long-Life/Condensed Milk	[✂]	[✂]	[✂]	[✂]	[✂]

IV. Insights on the Elasticity of Demand of Locally Produced Fresh Milk

- a. **Consumer Demand for Locally Produced Fresh Milk following Price Increases:** More than 97% of the respondents have stated that following the price increases announced by Benna on 23 July 2019, they intend to continue consuming locally produced fresh milk.
- b. **What would be the market response if the price of locally produced fresh milk had to increase by 10%? – A Counterfactual Analysis:** If the price of locally produced fresh milk had to increase by a further 10%, only [5-20]% of the respondents would switch to foreign milk products, while [5-20]% of the respondents answered that they would switch to condensed and/or long-life milk. These results complement the previous analysis and could also be an indication of strong brand loyalty towards the local product. Furthermore, [5-20]% of the respondents would reduce milk consumption while nearly [5-20]% would be willing to at least, try switching to condensed and/or long-life milk. The results are outlined in Table 9.

Table 9: Change in Consumer Behaviour in response to an increase of 10% in the price of locally produced fresh milk

%	Highly Unlikely (1)	Unlikely (2)	Neutral (3)	Likely (4)	Highly Likely (5)
Switch to foreign fresh milk products	[✂]	[✂]	[✂]	[✂]	[✂]
Switch to Condensed/Long-Life Milk	[✂]	[✂]	[✂]	[✂]	[✂]
Reduce the overall consumption of milk	[✂]	[✂]	[✂]	[✂]	[✂]
Be willing to at least, try switching for Condensed/Long-Life Milk	[✂]	[✂]	[✂]	[✂]	[✂]

- c. **What would be the market response if the price of locally produced fresh milk had to increase by 20%? – A Counterfactual Analysis:** If the price of locally produced fresh milk had to increase by a further 20%, [10-25]% of the respondents would switch to foreign fresh milk products while [5-20]% of the respondents would switch to condensed and/or long-life milk. As expected, while consumers' response is still expected to be relatively weak in the face of a further 20% increase in prices, however, the change in consumer behaviour is stronger than the case of the 10% increase in price. [10-25]% of the respondents would reduce milk consumption overall while nearly [10-25]% would be willing to at least, try switching to condensed and/or long-life milk. The results are outlined in Table 10.

Table 10: Change in Consumer Behaviour in response to an increase of 20% in the price of locally produced fresh milk

%	Highly Unlikely (1)	Unlikely (2)	Neutral (3)	Likely (4)	Highly Likely (5)
Switch to foreign fresh milk products	[✂]	[✂]	[✂]	[✂]	[✂]
Switch to Condensed/Long-Life Milk	[✂]	[✂]	[✂]	[✂]	[✂]
Reduce the overall consumption of milk	[✂]	[✂]	[✂]	[✂]	[✂]
Be willing to at least, try switching for Condensed/Long-Life Milk	[✂]	[✂]	[✂]	[✂]	[✂]

- d. **What would be the market response if the price of locally produced fresh milk had to increase by 10% while at the same time, the price of Condensed/Long-Life Milk decreases by 5%? – A Counterfactual Analysis:** If the price of locally produced fresh milk had to increase by a further 10% while at the same time the price of Condensed and Long-Life milk decreases by 5%, [10-25]% of the respondents would switch to foreign fresh milk products

while [5-20]% of the respondents would switch to condensed and/or long-life milk. It is noteworthy that the market for locally produced fresh milk is affected more when compared to the 10% price increase counterfactual but less in comparison to the 20% increase counterfactual. Moreover, [5-20]% of the respondents would reduce milk consumption overall, while nearly [5-20]% would be willing to at least, try switching to condensed and/or long-life milk. The results are outlined in Table 11.

Table 11: Change in Consumer Behaviour in response to an increase of 10% in the price of locally produced fresh milk and a decrease of 5% in the price of Condensed/Long-Life Milk

%	Highly Unlikely (1)	Unlikely (2)	Neutral (3)	Likely (4)	Highly Likely (5)
Switch to foreign fresh milk products	[✂]	[✂]	[✂]	[✂]	[✂]
Switch to Condensed/Long-Life Milk	[✂]	[✂]	[✂]	[✂]	[✂]
Reduce the overall consumption of milk	[✂]	[✂]	[✂]	[✂]	[✂]
Be willing to at least, try switching for Condensed/Long-Life Milk	[✂]	[✂]	[✂]	[✂]	[✂]

- e. **Maximum Price which consumers are willing to pay to continue consuming locally produced fresh milk (per litre):** Nearly 28% of the respondents highlighted that the maximum price that they are willing to pay for a 1 litre of locally produced fresh milk is [✂]. Nearly one-fourth of the respondents have indicated a price which is even higher than [✂] while another one-fourth indicated that the maximum price that they are willing to pay is the current price.
- f. **Maximum Price which consumers are willing to pay to continue consuming locally produced fresh milk (per litre) before considering switching to Condensed/Long-Life milk:** Nearly 65% of the respondents highlighted that the maximum price that they are willing to pay for a 1 litre of locally produced fresh milk before considering switching to condensed/long-life milk is in excess of [✂]. 7.3% of the respondents indicated a price of [✂] while nearly 5% highlighted the current price.

b. Decision of the Office on the Relevant Product Market

101. Taking the above into consideration, one can note substantial differences between the different types of milk, especially between fresh milk and long-life milk. These differences are synthesised in subsequent paragraphs.
102. From a demand-side perspective, the OFC notes the following differences:
- i. Texture: Long-life milk is also known as full cream or whole milk. This is because it gets a rich and creamy consistency from processing. Fresh milk, on the other hand, has a regular thin texture and appears more liquid than long-life milk (Friesland Foods/Campina).
 - ii. Longer usability and shelf life: Heightened temperatures of treatment used in long-life milk ensure that there is a greater and almost complete reduction in bacteria and heat-resistant enzymes which is not achieved through pasteurization of fresh milk. This gives UHT milk a longer shelf life.
 - iii. Health considerations: In the process of pasteurizing fresh milk, it is ensured that pathogenic bacteria are killed. However, it does not guarantee that other bacteria that can spoil milk are also killed. On the other hand, the treatment for long-life milk ensures that all bacteria are killed.
 - iv. Convenience: Fresh milk needs to be bought almost every two to three days, whereas long-life milk saves everyone regular trips to the market. While long-life milk can be purchased and stored for long stretches of time, however once opened, it has to be kept in the fridge and used within one week.
 - v. Taste: The process of pasteurization does not alter the taste of fresh milk. It tastes the same as it would have without treatment. On the other hand, long-life milk develops a distinct flavour of milk because of the process of sterilisation it undergoes.
 - vi. Storage: Fresh milk needs to be stored in cool temperatures. On the other hand, because of the treatment that long-life milk undergoes, long-life milk does not necessitate specialised storage care when storing. It can be kept at room temperature.
103. Notwithstanding this, although there are prime differences in the texture, taste, storage, usability and convenience, it is the view of the OFC that there are no differences in the nutritional values between fresh milk and long-life milk. This is because the prime nutrients of milk i.e. protein, fat, lactose and minerals are not at all made different or harmed by either pasteurization or sterilisation.
104. Furthermore, literature also points to important differences between the determinants of consumer behaviour for fresh milk and long-life milk. The fact that packaging (Krešić et al., 2010; Bonaventure and Umberger, 2012; Kuma et al., 2012; Yayar, 2012; Adam and Ali, 2014), brand (Hsu and Line, 2006; Alwis et al., 2009; Krešić et al., 2010; Bonaventure and Umberger, 2012; Tuan et al., 2013; Kumar and Babu, 2014; Bingham et al., 2014), design (Alwis et al., 2009; Adam and Ali, 2014), taste (Nagyová et al., 1998; Hsu and Lin, 2006; Nagyová et al., 2007; Alwis et al., 2009), habit formation (Nagyová et al., 1998; Alwis et al., 2009; Krešić et al., 2010; Bonaventure

and Umberger, 2012; Tuan et al., 2013; Kumar and Babu, 2014; Bingham et al., 2014), advertising (Nagyová et al., 1998; Tuan et al., 2013; Kumar and Babu, 2014), motivation and perception (Bonaventure and Umberger, 2012; Santoso et al., 2012; Trung et al., 2014), country of origin (Krešić et al., 2010; Tuan et al., 2013; Trung et al., 2014) and pricing (Nagyová et al., 1998; Hatirli et al., 2004; Alwis et al., 2009; Krešić et al., 2010; Kuma et al., 2012; Senadisai et al., 2014; Kumar and Babu, 2014; Bingham et al., 2014) have all been found to be key determinants of consumer behaviour for milk, amongst others, and given that there are key differences in these factors between fresh milk and long-life milk confirms that from a demand-side perspective, one cannot include fresh milk and long-life milk in the same relevant market.

105. On the other hand, from a supply-side perspective, the OFC notes that there exist the following differences:

- i. Processing and Treatment: The processing used for fresh milk is different from that used for long-life milk. Fresh milk requires mild pasteurization at a temperature of about 72 degrees Celsius for about 15 seconds whereas long-life milk is treated at an ultra-high temperature of about 130 to 140 degrees Celsius for about two seconds. To this end, the processing plant and processing equipment required for producing fresh milk and long-life milk are different.
- ii. Packaging: Fresh milk has regular packaging whereas long-life milk is packaged aseptically, which is to be packed using methods to avoid infection by pathogenic microorganisms.
- iii. Distribution and Storage: The transportation and storage of fresh milk necessitate refrigerated vehicles and refrigerators. On the other hand, long-life milk does not require refrigeration.

106. Potential competition “is not taken into account when defining markets, since the conditions under which potential competition will actually represent an effective competitive constraint depend on the analysis of specific factors and circumstances related to the conditions of entry”.⁷¹ In fact, potential competition is analysed in detail in the subsequent paragraphs of this report.

107. As noted in *United Brands v Commission*:

‘For the banana to be regarded as forming a market which is sufficiently differentiated from other fruit markets it must be possible for it to be singled out by such special features distinguishing it from other fruits that it is only to a limited extent interchangeable with them and is only exposed to their competition in a way that is hardly perceptible.’⁷²

108. After carefully examining the evidence in particular, the different views conveyed by MDP relative to the survey findings and the evidence from case law and market studies, the OFC considers fresh milk to constitute a separate product market from long-life and concentrated milk. Hence, for the purpose of this decision, the relevant product market constitutes unflavoured fresh milk.

⁷¹ Commission Notice on the definition of the relevant market for the purposes of Community competition law (97/C 372/03), paragraph 24.

⁷² *United Brands v Commission*. Case 27/76. Court of Justice, [1978] 1 CMLR 429, paragraph 22.

109. As highlighted by the Competition Appeal Tribunal in the case *Genzyme Limited v Office for Fair Trading*, ‘although, as the Tribunal said in *Aberdeen Journals (No.1)*, at paragraphs 103 and 104, contemporary documents showing how an undertaking views its competitors may constitute important evidence on the question of market definition, each case depends on its own factual circumstances. In that case the internal documents evidencing predatory conduct by *Aberdeen Journals* were relevant on the facts. In this case, **however, we do not think the rather general comments on the TKT website undermine our conclusions that in this case the specific relevant market for the purpose of assessing dominance is that of drugs for the treatment of Gaucher disease.**⁷³ [Emphasis Added]
110. As a result, although the OFC took note of the submissions by MDP, this should not in any way hinder the OFC’s independence when delineating the relevant market.

d. The Relevant Geographic Market

111. The EC defines the relevant geographic market as ‘comprising the area in which the undertakings concerned are involved in the supply and demand of products or services, in which the conditions of competition are sufficiently homogeneous, and which can be distinguished from neighbouring areas because the conditions of competition are appreciably different in those area’.⁷⁴
112. As highlighted by the EC in *Nederlandsche Banden Industrie Michelin v Commission*: ‘...dealers established in the Netherlands obtain their supplies only from suppliers operating in the Netherlands. The Commission was therefore right to take the view that the competition facing *Michelin NV* is mainly on the Netherlands market and that it is at that level that the objective conditions of competition are alike for traders.’⁷⁵
113. Similarly, the production of fresh milk in Malta takes place locally and fresh milk is distributed widely across the Maltese islands. Moreover, the sale of local fresh milk only takes place in the Maltese islands.
114. As a result, for the purposes of this investigation, the OFC determined the relevant geographic market to be the national territory of Malta. The OFC has also previously considered the relevant geographic market to be restricted to the national territory of Malta.⁷⁶

⁷³ *Genzyme Limited v Office for Fair Trading* (1016/1/1/03). Competition Appeal Tribunal, [2004] CAT 4, [2004] Comp.A.R. 358, paragraph 217.

⁷⁴ Commission Notice on the definition of the relevant market for the purposes of Community competition law (97/C 372/03), paragraph 8.

⁷⁵ *Nederlandsche Banden Industrie Michelin v Commission*. Case 322/81. Court of Justice, [1983] ECR 3461, [1985] 1 CMLR 282, paragraph 26.

⁷⁶ COMP/CCD/7/11 – Alleged infringement by Malta Dairy Products Limited of Article 9 of the Competition Act with regards to the excessive pricing of milk products, page 9.

C. Dominance

115. According to the *Guidance on Article 102 Enforcement Priorities* issued by the EC, the assessment of dominance should consider the competitive structure of the market, and in particular the following factors:

- a. constraints imposed by the existing supplies from, and the position on the market of, actual competitors (the market position of the dominant undertaking and its competitors),
- b. constraints imposed by the credible threat of future expansion by actual competitors or entry by potential competitors,
- c. constraints imposed by the bargaining strength of the undertaking's customers (countervailing buyer power).⁷⁷

116. Each factor is analysed in detail in the below paragraphs.

a. The Market Position of the Dominant Undertaking and its Competitors

117. As held in *Hoffmann-La Roche & Co. v Commission*, a dominant position enables an undertaking 'to prevent effective competition being maintained on the relevant market by affording it the power to behave to an appreciable extent independently of its competitors, its customers and ultimately of the consumers.'⁷⁸

*'Such a position does not preclude some competition, which it does where there is a monopoly or a quasi-monopoly, but enables the undertaking which profits by it, if not to determine, at least to have an appreciable influence on the conditions under which that competition will develop, and in any case to act largely in disregard of it so long as such conduct does not operate to its detriment.'*⁷⁹

118. As held in *Hoffmann-La Roche & Co. v Commission*, very large market shares which are sustained for some time are in themselves, and save in exceptional circumstances, evidence of dominance.⁸⁰

119. According to submissions made by MDP, 'we are not aware of any grocery retail outlets that do not stock Benna fresh Milk at all, although MDP is unlikely to know every retail outlet in Malta and Gozo. On the other hand, MDP is aware that there are various such outlets that do not stock the full range of Benna fresh milk products.'⁸¹

120. The OFC opines that it is highly unlikely that small- and/or medium-sized grocery retail outlets have adequate refrigerated shelf space to supply a range of fresh milk products other than

⁷⁷ Commission Notice on Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings. (2009/C 45/02), paragraph 12.

⁷⁸ *Hoffman La Roche & Co. v Commission*. Case 85/76. Court of Justice, [1979] ECR 461, [1979] 3 CMLR 211, paragraph 38.

⁷⁹ *Ibid*, paragraph 39.

⁸⁰ *Ibid*, paragraph 41.

⁸¹ Source: MDP submissions, dated 19 November 2019.

those supplied by MDP. Notwithstanding this, if there are any small- and/or medium-sized grocery retail outlets⁸² that do so, the OFC is resting on the assumption that their level of sales attributed to fresh milk products other than those pertaining to MDP are unlikely to have a large effect on the market shares of MDP.

121. On the other hand, the OFC opines that large-sized grocery retail stores having a sales area exceeding 200 square meters and a wider product range when compared to small- and medium-sized grocery retail outlets have the facilities and adequate floor space to supply a wider range of fresh milk products other than those supplied by MDP. As a result, basing its assessment on the analysis carried out in concentration decision COMP/MCCAA/01/2020⁸³, the OFC selected a sample of the largest grocery retail stores in Malta and sent an RFI requesting undertakings to indicate whether they supply or have supplied fresh milk products other than those supplied by MDP over the last four years and if in the affirmative, provide sales data pertaining to fresh milk products. The request for information was sent on 11 September, 2020 to the following undertakings: Lidl Malta Ltd, Park Towers, Lasco Supermarket, Valyou Supermarket, Trolees Supermarket, Scotts Supermarket, PG Group (Pavi and Pama), Arkadia Supermarkets, Chain Supermarkets, Iceland Supermarkets, Greens Supermarket and Smart Supermarket.
122. Collectively, the above-mentioned stores cover an estimated [redacted] of all the turnover registered in the grocery sector in Malta in 2018⁸⁴ and over [redacted] of all the turnover registered by large-sized grocery retail stores in Malta. As a result, it is the OFC opinion that the sub-sample selected is representative of the large grocery store sector in Malta.
123. In their reply, [redacted] confirmed that they never supplied any other fresh milk products except those supplied by MDP over the period under review. On the other hand, [redacted] noted that the percentage of non-MDP fresh milk products sold as a proportion of total fresh milk products sales over the period under review is less than [redacted] both in terms of volumes and in terms of values, with the exception of [redacted] whose sales values marginally exceed [redacted].
124. [redacted] highlighted that over the period under review, the percentage of non-MDP fresh milk products sold as a proportion of total fresh milk products sales stood at [redacted] in terms of volumes and [redacted] in terms of values. The highest proportions were recorded by [redacted], who recorded percentage figures for both volumes and values in the region of [redacted].
125. By means of extrapolation analysis and with reference to concentration decision COMP/MCCAA/01/2020⁸⁵ issued by the OFC, based on the market shares inferred in the said concentration decision on 2018 data as proxies for the size of the above-mentioned supermarkets in the period under review, one can estimate the market share of MDP attributed to fresh milk sales recorded in the large-sized grocery retail store segment to total [75-100]% and [75-100]% in terms of volumes and values, respectively, and [75-100]% of total fresh milk sales in terms of volumes and values in the grocery retail market in Malta.

⁸² The definitions adopted with respect to the size of grocery stores are as per concentration decision COMP/MCCAA/01/2020 taken by the OFC on 5 June 2020.

⁸³ Ibid.

⁸⁴ Estimates based on the data collected by the OFC for concentration decision COMP/MCCAA/01/2020. Ibid.

⁸⁵ Ibid.

126. As held in *AKZO Chemie BV v Commission*, ‘with regards to market shares the Court has held that very large shares are in themselves, and save in exceptional circumstances, evidence of the existence of a dominant position...That is the situation where there is a market share of 50% such as that found in this case.’⁸⁶

127. Retention of market share may result from effective competition and is not – by itself – an indicator of dominance. However, when dominance is established, the retention of market share supports the conclusion that the position of dominance has been maintained.⁸⁷

128. The existence of a dominant position may depend on a combination of factors, where no single one is necessarily decisive.⁸⁸ Other factors indicating dominance include the disparity between the market share of the leading undertaking and the next largest competitor, the technological lead of an undertaking over its competitors, the existence of a highly developed sales network, barriers to entry and the absence of potential competition.⁸⁹

b. Barriers to Entry and Expansion

129. In identifying whether MDP holds a dominant position in the relevant market, it is necessary to conduct an evaluation of any barriers to expansion or entry. This is due to the fact that an undertaking with high market shares is unlikely to be able to behave independently of any of its stakeholders in a market where such barriers are low.

130. Barriers to entry and expansion can take various forms. They may be regulatory barriers or may take the form of advantages specifically enjoyed by the dominant undertaking. They may also include costs and other impediments resulting from network effects or significant investments by the dominant undertaking which makes it hard for potential entrants or competitors to match. Persistently high market shares may be indicative of the existence of barriers to entry and expansion.

131. This section analyses these barriers to entry and expansion in more detail.

I. Regulatory Barriers

132. Regulatory requirements may restrict the potential entry of new undertakings, thereby constituting barriers to entry. In order for a new entrant to obtain licensing to operate a dairy production plant, apart from the specific construction regulatory requirements required for buildings intended to be used as dairy plants, there are also the food safety requirements which must be adhered to when operating.

⁸⁶ *AKZO Chemie BV v Commission*. Case C-62/86. Court of Justice, [1991] ECR I-3359, 1993 5 CMLR 215, paragraph 60.

⁸⁷ *Hoffman La Roche & Co. v Commission*. Case 85/76. Court of Justice, [1979] ECR 461, [1979] 3 CMLR 211, paragraph 44.

⁸⁸ *United Brands v Commission*. Case 27/76. Court of Justice, [1978] 1 CMLR 429, paragraphs 127 and 128.

⁸⁹ *Ibid*, paragraph 48.

133. In fact, EU regulations necessitate that incoming raw milk is of high quality. Apart from that, the dairy processing plant needs to be equipped with high quality processing and manufacturing equipment, which equipment needs to be certified by the competent authorities.

134. To date, there is only one other local company of a certain size which has been given a license as a processing plant for raw milk. However, this company is not active in the market of fresh milk. Apart from this company, there are some other small manufacturers which have been granted a license to produce other fresh milk products such as Maltese cheese.

II. Economic Advantages

135. Various economic advantages have been considered to be barriers to entry and expansion:

i. Economies of scale and scope

136. Entrants potentially entering the market of fresh milk where the incumbent enjoys large economies of scale would require entering the market on a large scale in order to be able to compete effectively.

137. The ECJ considered economies of scale to be a relevant factor in *United Brands*⁹⁰, and the EC referred to this matter specifically in *Amazon*⁹¹; economies of scope are treated in the same way.

138. MDP has been in the market for a considerable number of years and has also invested in expanding its range of products to include ricotta, mozzarella and butter amongst others, thereby benefitting from economies of scale and scope. To this end, potential entrants would take time to reach the same position as that of MDP and would as a result find it difficult to benefit from such economies of scale and scope as those enjoyed by MDP.

ii. Developed Sales Network

139. In *Hoffmann-La Roche*⁹², the ECJ pointed to Roche's developed sales network as a relevant factor conferring upon it commercial advantages over its rivals. The EC has treated both vertical integration and the benefit of well-established distribution systems as a barrier to entry in several other decisions⁹³, since this would impede access for a would-be entrant to the market.

140. In the case of MDP, given its considerable number of years of market presence, one could regard MDP's sales network as well developed. As submitted by MDP, the company is not aware of any grocery retail outlets that do not stock Benna's Fresh Milk.⁹⁴ As a result, the OFC regards MDP's sales network to be well developed.

⁹⁰ *United Brands v Commission*. Case 27/76. Court of Justice, [1978] 1 CMLR 429.

⁹¹ European Commission commitment decision of 4 May 2017, para 65(3).

⁹² *Hoffman La Roche & Co. v Commission*. Case 85/76. EU:C:1979:36, paragraph 48.

⁹³ See for example *Napier Brown – British Sugar* OJ [1988] L 284/41, paragraph 56.

⁹⁴ Source: MDP submissions, dated 19 November 2019.

141. In addition, MDP is vertically integrated both with raw milk producers and also with the distributors and the retailers. In fact, MDP has bilateral agreements with each raw milk producer and with each distributor responsible for distributing Benna's products. MDP is also active in distributing its products directly to some of the retailers. As a result, the OFC opines that MDP has a well-established distribution system. To this end, it must be emphasised that the bilateral agreements that MDP has with each distributor do not preclude the distributors from distributing other products not under Benna's umbrella.

iii. First-Mover Status

142. In *Astra Zeneca*⁹⁵, the General Court and the European Commission considered AZ's first-mover status to be a factor indicating dominance. Given that MDP is the only player and thus the first-mover in the local market when it comes to fresh milk production, the OFC shares the views of the General Court and the EC in this respect.

iv. Integration of MDP's activities

143. In *United Brands*⁹⁶, the ECJ described the extent to which UBC's activities were integrated – it owned banana plantations and transport boats and it marketed its bananas itself – and said that this provided that firm with commercial stability which was a significant advantage over its competitors.

144. MDP also enjoys the integration of a number of activities that are required to deliver the product to the final-end consumer.

145. KPH holds 70 per cent shareholding of MDP and over the years, its members developed a strong and efficient supplier-buyer relationship. This ensured total quality control over the milk supply chain with KPH as the sole owner of the feed mill supplying animal feed to its members.

146. Furthermore, MDP is also active in the distribution phase of its products. MDP's products are distributed by itself in conjunction with 36 other independent distributors. MDP is also responsible for its own marketing campaigns.

147. Like *United Brands*, this gives MDP a significant advantage over its actual and potential competitors.

v. Advertising and Brand Image

148. In *United Brands*⁹⁷, the ECJ considered that *United Brand's* advertising campaign and brand image were significant factors indicating dominance. *United Brands* had spent considerable resources establishing the *Chiquita* brand name, which was well protected by trademarks. In its second *Michelin*⁹⁸ decision, the EC relied upon the indisputable quality and reputation of the *Michelin* tyre brand in its finding of dominance. Furthermore, the EC has noted that advertising

⁹⁵ Case T-321/05 EU:T:2010:266, paragraphs 276-283.

⁹⁶ *United Brands v Commission*. Case 27/76. Court of Justice, [1978] 1 CMLR 429, paragraphs 69-81 and 85-90.

⁹⁷ *Ibid*, paragraphs 91-94.

⁹⁸ *Michelin* OJ [2002] L 143/1, paragraph 184.

expenditure could make entry difficult into the market for fast-moving consumer goods such as soft drinks.⁹⁹

149. MDP has undertaken major investments in expanding and diversifying its product portfolio to include a new range of milk drinks, introduction of pasteurised fresh cheeselets and new diversified range of yoghurts and desserts amongst others. Furthermore, MDP has also undertaken an extensive rebranding exercise to strengthen and enhance the brand image of the local fresh milk product and has invested heavily in promotional campaigns and marketing.
150. Furthermore, in line with the findings of the EC, the fact that such advertising expenditure is happening in a market which involves fast-moving consumer goods further strengthens dominance.

III. Sunk Costs of Entry

151. Potential entrants in the production of fresh milk products incur costs which cannot be recovered upon exiting the market. A considerable level of sunk costs constitutes a barrier to entry and as a result stifles potential competition.
152. In opening and operating a dairy processing plant to produce fresh milk and other fresh milk products, the entrant is required to undertake substantial capital investment. According to MDP submissions, it is estimated that the costs incurred in construction and civil works related to the building of a dairy processing plant of [X] are significant. Furthermore, the entrant would then need to invest in processing equipment, manufacturing and plant utilities and other costs related to software automation, design, insurance etc. Overall, these are estimated to amount to around [X].¹⁰⁰
153. In addition, such equipment and utilities need to be constantly updated in order to meet new regulatory requirements and improve the quality of production. In fact, MDP has undertaken considerable investments as part of its restructuring program to upgrade the facilities at MDP's production plant, reaching more than €17 million in 2013.¹⁰¹
154. As a result, the incurrence of such substantial costs and the lengthy timelines involved in opening and operating a dairy processing plant makes an effective entry in the market difficult in the short- to medium-run.

IV. Potential Competition

155. Perhaps, it could be argued that the other local companies which are mainly active in the production of fresh milk products such as ricotta and fresh and dry cheeselets could potentially be capable of start producing fresh milk.

⁹⁹ Case M 190 Nestle/Perrier OJ [1992] L 356/1.

¹⁰⁰ Source: MDP submissions, dated 19 November 2019.

¹⁰¹ P. Von Brockdorff (2002), *Development and Agri-Food Policies in the Mediterranean Region (Malta Report)*, CIHEAM Annual Report 2002, Paris: Presses de Sciences Po.

156. While the raw milk capacity required to produce fresh milk is much larger than that of the other fresh milk products, apart from present supply-side constraints, there is a slight chance that MDP could be constrained from acting completely independently of its potential local competitors in the dairy processing market.
157. Furthermore, MDP could potentially face higher competition in the catering sector. The fact that the catering sector is *a priori* much more cost sensitive than the rest of the market makes MDP more prone to lose its market share in this segment.
158. Furthermore, MDP could also potentially face higher competition from foreign fresh milk products such as those manufactured in Sicily. Retailers who could afford to import fresh milk products from abroad constitute the highest potential threat to the local fresh milk product.

c. Countervailing Buyer Power

159. Competitive constraints may be exerted not only by actual or potential competitors but also by customers.¹⁰² Even an undertaking with a high market share may not be able to act to an appreciable extent independently of customers with sufficient bargaining strength.¹⁰³ This may be attributed to the customers' size or their commercial significance for the dominant undertaking, and their ability to switch quickly to competing suppliers, to promote new entry or to vertically integrate, and credibly threaten to do so. If countervailing buyer power is sufficient, it could deter the dominant undertaking to profitably increase prices. However, if only a particular or limited segment of customers is shielded from the market power of the dominant undertaking, then buyer power is not considered a sufficiently effective constraint.¹⁰⁴
160. Downstream to MDP, there are the distributors who are in charge of distributing the products of MDP and the retailers who make the product available to the final-end consumer.
161. The OFC opines that the distributors are in a position to bargain with MDP in the purchase of fresh milk in cartons. The fact that the distributors who are in charge of distributing MDP's products have formed groups and joined unions strengthens their countervailing buyer power.
162. With respect to the retail market, according to submissions by MDP dated 19 November 2019, MDP is not aware of any retailers that do not supply the products of MDP. As a result, the final-end consumer is faced with a healthy choice set of retailers from where he/she can buy the products supplied by MDP. However, according to a survey conducted by MaltaToday in 2016¹⁰⁵, when consumers were asked from which supermarkets they buy most, LIDL Malta Ltd achieved a share of 48.6% compared to the second highest with a share of 15.4%. While respondents were allowed to refer to more than one supermarket, nevertheless, this does not reduce the strong position of LIDL in the grocery retail market in Malta.

¹⁰² Commission Notice on Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings. (2009/C 45/02), paragraph 18.

¹⁰³ Irish Sugar v Commission. Case T-228/97. Court of Justice, [1999] ECR II-2969, paragraphs 97 -104.

¹⁰⁴ Commission Notice on Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings. (2009/C 45/02), paragraph 18.

¹⁰⁵ MaltaToday Survey | Lidl is Malta's most popular supermarket, accessed on 14 November 2019. Available from: <https://www.maltatoday.com.mt/news/data_and_surveys/69499/maltatoday_survey__lidl_is_maltas_most_popular_supermarket#.XcOq0ldKiUk>.

163. In fact, according to the calculations of the OFC, it is estimated that LIDL accounted for approximately [redacted] of the volume of sales of MDP's fresh milk 2.5% fat and [redacted] of the volume of sales of MDP's Skimmed Milk in 2018.¹⁰⁶

164. According to submissions by LIDL Malta Ltd. dated 29 August 2019, [redacted].¹⁰⁷

165. In *Motorola*¹⁰⁸, the EC emphasised that one of the key elements of countervailing buyer power is a buyer's ability to switch to competing suppliers, which Apple lacked in that case.

166. In this case, as also highlighted by LIDL Malta Ltd in their submissions, [redacted].

167. Given the fact that LIDL Malta Ltd accounts for a [redacted] share of MDP's sales volume puts [redacted].

d. Economic Profitability

168. As held in *United Brands v Commission*, 'an undertaking's economic strength is not measured by its profitability; a reduced profit margin or even losses for a time are not incompatible with a dominant position, just as large profits may be compatible with a situation where there is effective competition. The fact that UBC's profitability is for a time moderate or nonexistent must be considered in the light of the whole of its operations.'¹⁰⁹

169. An analysis of MDP's profitability in the last years is provided in the table below:

Table 12: MDP's operating profit or loss for the period 2012 to 2018

	2012	2013	2014	2015	2016	2017	2018
Operating Profit / (Loss)	[redacted]						
Profit/Sales Ratio	[redacted]						

Source: MDP submissions, dated 2 September 2019.

170. As can be seen from this table, over the period 2012 to 2018, when excluding income tax expense and investment income, MDP registered an operating loss in 2012, 2013 and 2018 and an operating profit in the remaining years.

171. Notwithstanding this, as highlighted in *United Brands*, 'the finding that, whatever losses UBC may make, the customers continue to buy more goods from UBC which is the dearest vendor,

¹⁰⁶ Source: MDP submissions; LIDL Malta Ltd. Submission; author's calculations.

¹⁰⁷ Source: Submissions by LIDL Malta Ltd.

¹⁰⁸ Case AT. 39985 – Motorola – Enforcement of GPRS Standard Essential Patents. Commission decision of 19 April 2014, paragraphs 237-268.

¹⁰⁹ *United Brands v Commission*. Case 27/76. Court of Justice, [1978] 1 CMLR 429, paragraphs 126 and 127.

*is more significant, and this fact is a particular feature of the dominant position and its verification is determinative in this case.*¹¹⁰

e. Conclusion on Dominance

172. Taking the above into consideration, the OFC considers MDP to be have a quasi-monopoly and therefore in a dominant position in the market under assessment.

173. At this stage, the OFC will refrain from analysing as to whether the distributors and the retailers are either on an individual level or jointly dominant, each in their respective categories. Notwithstanding this, such analysis will be conducted subsequently if it results that there is evidence of excessive and/or unfair pricing at the distribution or at the retailer level.

¹¹⁰ United Brands v Commission. Case 27/76. Court of Justice, [1978] 1 CMLR 429, paragraph 128.

Section 3: Abuse

A. Introduction

174. The conduct subject of this ex-officio investigation is to determine whether the actual price increases of Benna fresh milk products are the result of an abuse of a dominant position in accordance with Article 9(2)(a) of the Competition Act and Article 102(a) of the TFEU.
175. Article 9 of the Competition Act prohibits any abuse by one or more undertakings of a dominant position within Malta or any part of Malta. In particular, Article 9(2)(a) states that one or more undertakings shall be deemed to abuse of a dominant position, where it or they directly or indirectly impose an excessive or unfair purchase or selling price or other unfair trading conditions.
176. In order to establish that there has been a breach of Article 9(2)(a) of the Competition Act and/or Article 102(a) of the TFEU, the OFC must demonstrate that the market players investigated along the fresh milk supply chain namely MDP, the distributors and the retailers distributing and selling Benna's fresh milk products are indeed undertakings.
177. Article 2 of the Maltese Competition Act defines an undertaking as: '*any person whether an individual, a body corporate or unincorporated or any other entity, pursuing an economic activity, and includes a group of undertakings.*'
178. MDP, holder of company registration number C 7833, satisfies this definition since it is carrying out an economic activity involving the processing, packaging and distribution of fresh liquid milk and milk products.
179. The thirty-six distributors who are entrusted by MDP to distribute and sell Benna's branded products to its customers are also classified as undertakings since they are also carrying out an economic activity.
180. Finally, the grocery retail outlets in Malta are also defined as an undertaking since they are also carrying out an economic activity, that of offering a platform to final-end customers to purchase grocery products.
181. In order to establish that there has been a breach of Article 9(2)(a) of the Competition Act and/or Article 102(a) of the TFEU, the OFC must demonstrate that the undertaking/s in question: (i) holds a dominant position in the relevant market; and (ii) has abused from that dominant position.
182. While the issue of the dominant position has been tackled in the previous chapter, in order to establish that there has been a breach of Article 9(2)(a) of the Competition Act and/or Article 102(a) of the TFEU, it must be demonstrated that there has been an abuse of that position.
183. In *Tetra Pak v Commission case*, the EU's General Court in its judgment has held that the scope of the special responsibility imposed on a dominant undertaking must be considered in light of the specific circumstances of each case, reflecting the fact that competition is weakened as a result of the very presence of that undertaking on the market.¹¹¹

¹¹¹ Judgment in *Tetra Pak v Commission Case*, T-83/91, EU:T:1994:246, paragraphs 114 and 115.

184. In *United Brands*, the Courts of Justice of the EU held that:

*'...charging a price which is excessive because it has no reasonable relation to the economic value of the product supplied would be such an abuse.'*¹¹²

185. In order to determine excessive pricing, the Court of Justice held in *United Brands* that the following cumulative two-stage test (the 'United Brands Test') could be used to establish whether a price had no reasonable relation to the economic value of the product supplied:

- i. *'whether the difference between the costs actually incurred and the price actually charged is excessive'* and, if yes
- ii. *'whether a price has been imposed which is either unfair in itself or when compared to competing products.'*¹¹³

186. The EC stressed that the two stages outlined in *United Brands* must be satisfied to prove excessive pricing: *'While a comparison of prices and costs, which reveals the profit margin, of a particular company may serve as a first step in the analysis, this in itself cannot be conclusive as regards the existence of an abuse under Article 82 [102].'*¹¹⁴

187. The application of the *United Brands* test to a particular set of data involves a *'...considerable margin of appreciation.'*¹¹⁵

188. The judgment of the Court of Justice of the EU in *United Brands* is *'the seminal judgment in this area of the law...'*¹¹⁶. The ECJ identified several steps to establishing an unfairly high price which may be summarised as follows:

- i. an analysis of the costs incurred in producing the product or service;
- ii. a comparison of those costs with the price charged and an assessment of whether the resulting difference, i.e. the profit, is such that the price charged is excessive; and if so
- iii. an assessment of whether the excessive price bears no reasonable relation to the economic value of the product or service supplied and is an abuse of a dominant position, with the consequence that it is either:
 - a. unfair in itself; or
 - b. unfair when compared with competing products.¹¹⁷

¹¹² *United Brands v Commission*. Case 27/76. Court of Justice, [1978] 1 CMLR 429, paragraph 250. In this respect, see also judgments in *General Motors Continental NV v Commission* C-26/75, EU:C:1975:150, paragraph 12.

¹¹³ *United Brands v Commission*. Case 27/76. Court of Justice, [1978] 1 CMLR 429, paragraph 252.

¹¹⁴ *Scandlines Sverige AB v. Port of Helsingborg*. Case COMP/A.36568/D3, paragraph 102.

¹¹⁵ *Albion Water II*, paragraph 261.

¹¹⁶ *Ibid*, paragraph 14.

¹¹⁷ *Ibid*, paragraph 20.

189. As noted in *Albion Water II*, 'the above approach has consistently been applied by the Commission of the European Communities, the OFT, the Tribunal and the Court of Appeal.'¹¹⁸

190. As highlighted in the previous section, the OFC has demonstrated that MDP is in a dominant position but has refrained from analysing as to whether the distributors and the retailers are either on an individual level or jointly dominant, each in their respective categories. Given that a substantial portion of the final consumer price is earned by MDP from selling its focal product to the distributors¹¹⁹, and given that the remaining unaccounted portion is shared between the distributors and the retailers, unless otherwise stated, the assessment to determine whether the prices charged are the result of an abuse of a dominant position in accordance with Article 9(2)(a) of the Competition Act and Article 102(a) of the TFEU, focuses primarily on MDP.

191. Notwithstanding this, in line with EU jurisprudence, the OFC will also assess on a general level, the final consumer price charged for the focal product. If it results that the prices charged may indicate the possibility of an abuse, the OFC will assess dominance and abuse at each stage of the supply chain separately.

B. Legal Background: Excessive Pricing

192. The first step of the *United Brands Test* to assess whether a price charged by a dominant undertaking is unfairly high is to establish 'whether the difference between the costs actually incurred and the price actually charged is excessive.'¹²⁰

I. Costs

193. As highlighted in *United Brands*, the starting point in computing the *United Brands Test* is to measure 'the costs actually incurred'¹²¹ in supplying the product in question. These include:

- a. the costs directly incurred in supplying the product or service; and
- b. an appropriate apportionment of the indirect costs that are 'reasonably attributable'¹²² to the product or service.

194. There is no legally prescribed methodology for measuring cost in excessive pricing cases. In *Albion Water II*, the Competition Appeals Tribunal stated that, rather, 'it is a matter of fact, accounting technique and economic assessment.'¹²³

195. However, as stated in various case law, it is salient for the OFC to ensure that all costs that are incurred by the undertaking are adequately measured and captured.¹²⁴

¹¹⁸ Ibid, paragraph 21.

¹¹⁹ This is estimated to total 87% of the final consumer price with the exception of lactose free milk which share is marginally lower at nearly 80%.

¹²⁰ *United Brands v Commission*. Case 27/76. Court of Justice, [1978] 1 CMLR 429, paragraph 252.

¹²¹ Ibid.

¹²² *Albion Water II*, paragraph 198.

¹²³ Ibid, paragraph 88.

¹²⁴ Ibid. See also judgment in *Ministere Public v Tournier* C-395/87, EU:C:1989:319, paragraph 42.

II. Reasonable Rate of Return

196. In addition to capturing the costs incurred, it is normally necessary to allocate a reasonable rate of return on that amount and include it in the cost figure before comparing costs to the price actually charged.¹²⁵
197. The purpose of a reasonable rate of return is to acknowledge that an undertaking will require a financial incentive to engage in the activity of supplying a good or service, as a return on capital invested and/or as a reward for taking on any risks associated with these activities. As set out in *Genzyme Remedy*, ‘the determination of an appropriate margin is necessarily a question of judgment and appreciation’¹²⁶ and ‘the actual margin to be set is not a matter of precise mathematics.’¹²⁷
198. Determining what the OFC considers to be a reasonable rate of return is a necessary step in this analysis. The reasonable rate of return does not determine the maximum return an undertaking is permitted to earn on a product. It is possible for an undertaking to price above cost without those prices being found to be excessive or unfair.
199. The assessment of a reasonable rate of return needs to be determined on a case-by-case basis.¹²⁸ The fact that the OFC decides on a reasonable rate of return for one product or undertaking does not mean that it will necessarily be applicable for another undertaking supplying a different product, even if these are within the same industry.

III. Cost/Price comparison

200. Having established the costs incurred plus a reasonable rate of return, it is then necessary to assess whether the difference between cost plus and the price charged is excessive.
201. This assessment ‘involves a proper degree of discretionary judgment by the decision-maker’¹²⁹ and requires the exercise of judgment,¹³⁰ having regard to the specific circumstances of the individual case, in particular the specific features of the product concerned and competitive conditions in the relevant markets.
202. In *Albion Water II*, the Competition Appeal Tribunal, when applying the first stage of the *United Brands Test*, stated that:

‘We note that the Authority submitted that a price may not be ‘excessive’ within the meaning of the first United Brands question where the price exceeds costs but not by a material extent. While we are prepared to accept that a material difference between price and cost must be shown, we see

¹²⁵ *Albion Water II*, paragraph 89.

¹²⁶ *Genzyme Remedy*, paragraph 255.

¹²⁷ *Genzyme Remedy*, paragraph 279.

¹²⁸ Decision of the Competition and Markets Authority. Unfair Pricing in respect of the supply of phenytoin sodium capsules in the UK. Case CE/9742-13, 7 December 2016.

¹²⁹ *Albion Water II*, paragraph 193.

¹³⁰ *Albion Water II*, paragraph 194.

no need to specify, in this case, when a particular difference is sufficiently large to be deemed excessive.'

203. The following differences between the price charged and the costs incurred have been found to be excessive based on the specific facts of the following cases:

- a. In *Albion Water II*, the Competition Appeal Tribunal held that a price of 46.8% above the costs reasonably attributable to the product was material and excessive.
- b. In *Deutsche Post*, the EC found that a price 25% above the costs reasonably attributable to the product was excessive.¹³¹
- c. In the *Aspen case*, the Italian Competition Authority concluded that revenues were between 150 and 400% higher than a cost-plus price.¹³²

IV. Other important Benchmarks

204. In addition to the above cases, there were other cases of excessive pricing which did not necessarily resort restrictively to the cost-plus approach.

205. Since the price/cost analysis cannot always produce an answer to the question of whether a price is excessive, the ECJ in *United Brands*¹³³ and in *AKKA/LAA*¹³⁴ highlighted that there might be other ways of determining whether this is the case. Competition authorities can adopt a certain degree of flexibility with respect to the methodology to be followed when determining whether a price is excessive¹³⁵ and it may be sensible to combine different methods.¹³⁶

206. In *Scandlines Sverige AB v port of Helsingborg*¹³⁷, the EC rejected a complaint that port charges at the port of Helsingborg were excessively high. The EC carried out an extensive investigation of the costs incurred by the port. However, a simple 'cost-plus' approach was insufficient to establish that the prices were unfair, since it was also necessary to look at the economic value of the services provided.

207. The EC noted that ferry operators benefitted from the location of the port, a fact that was relevant to the economic value of the port services. The EC also looked to see if the port charges were unfair when compared with the prices charged for other services provided in the same port, and with the prices charged to ferry operators in other ports¹³⁸. The EC concluded that given that the burden of proving an abuse was upon it, there was no infringement of Article 102.

¹³¹ EC decision COMP/36.915. *Deutsche Post AG – Interception of cross border mail* [2001], paragraphs 166 and 167.

¹³² Autorità garante della concorrenza e del mercato (ICA), decision No. 26185, 29 Sept. 2016.

¹³³ Case 27/76 EU:C:1978:22, paragraph 253.

¹³⁴ Case C-177/16 EU:C:2017:689, paragraph 37.

¹³⁵ Case C-177/16 AKKA/LAA EU:C:2017:689, paragraph 49.

¹³⁶ See the AG's opinion in Case 177/16 AKKA/LAA EU:C:2017:286, paragraphs 43-45.

¹³⁷ Commission Decision of 23 July 2004; a second complaint against the port, by Sundbusserne, was also rejected.

¹³⁸ *Ibid*, paragraph 86.

208. In *Scandlines Sverige AB v port of Helsingborg*, the EC noted that while a comparison of costs and prices may serve as a first step in the analysis, this in itself cannot be conclusive as regards the existence of an abuse under Article 82.¹³⁹ Similarly, in *Attheraces*, the UK Court of Appeal said that evidence that a firm was pricing above cost did not provide sufficient evidence to conclude that prices were excessive: above cost pricing was held to be a necessary but not a sufficient condition for excessive pricing.¹⁴⁰
209. On the other hand, in *Deutsche Post AG – Interception of cross-border mail*¹⁴¹, the EC considered that Deutsche Post's prices for the onward transmission of cross-border mail were excessive. In doing so the EC said that, as it could not make a detailed analysis of Deutsche Post's costs, it would have to use an alternative benchmark to determine whether it was guilty of abuse;¹⁴² this it did by comparing Deutsche Post's prices for cross-border mail with its domestic tariff,¹⁴³ and it decided that there was indeed an abuse.
210. As a result, depending on the circumstances of the case, it may be appropriate to proceed on the basis of a comparison of the dominant undertaking's prices with an appropriate comparator, for example the prices of non-dominant firms, or the dominant firm at a different point in time, or the dominant firm in different geographical markets. Any chosen comparator must be selected in accordance with 'objective, appropriate and verifiable criteria', and the comparison must be made on a consistent basis¹⁴⁴.
211. As highlighted in *Scandlines Sverige AB v port of Helsingborg*¹⁴⁵, any comparator used for the assessment of whether an excessive price is unfair must be sufficiently similar to the product concerned in order for the comparison to be meaningful. For example, it might be possible to compare the dominant firm's price with the prices charged in:
- a. a neighbouring market for the same product¹⁴⁶,
 - b. a discrete segment of the relevant market¹⁴⁷,
 - c. another Member State¹⁴⁸,
 - d. an international benchmark¹⁴⁹.
212. The idea of using a comparator to establish whether prices are excessive was also used in *Lucazeau v SACEM*¹⁵⁰. The case concerned the level of royalties charged for the playing of recorded music in discotheques. The ECJ suggested that a comparison should be made with the level of fees charged in the other Member States.

¹³⁹ Ibid, paragraph 232.

¹⁴⁰ *Attheraces Ltd v British Horseracing Board Ltd* [2007] EWCA Civ 38; [2007] UKCLR 309, CA.

¹⁴¹ OJ [2001] L 331/40.

¹⁴² Ibid, paragraph 159.

¹⁴³ Ibid, paragraph 160-166.

¹⁴⁴ Case C-177/16 AKKA/LAA EU:C:2017:689, paragraph 38, 41, 44 and 51.

¹⁴⁵ Commission Decision of 23 July 2004.

¹⁴⁶ Case 30/87 *Corinne Bodson v Pompes Funebres* EU:C:1988:225.

¹⁴⁷ Case 1001/1/1/01 *Napp Pharmaceutical Holdings Ltd v Director General of Fair Trading* [2002] CAT 1.

¹⁴⁸ Case 395/87 *Ministere Public v Tournier* EU:C:1989:319.

¹⁴⁹ *Standard and Poor*, Commission decision of 15 November 2011.

¹⁵⁰ Case 110/88 EU:C:1989:326.

213. Similarly, in *AKKA/LAA*¹⁵¹, the ECJ stated that it was valid to determine the lawfulness of AKKA/LAA's prices by comparing them with those charged by collecting societies in the other Member States¹⁵² and went on to give guidance as to how a comparative analysis should be conducted in the circumstances of that case. It said that, to be unlawful, the prices would need to be significantly higher, and persistently so, when compared with prices in the other Member States¹⁵³.

214. The same methodology was also conducted by the EC in *United Brands*. The EC concluded that United Brands was charging excessive pricing based on a comparison of prices between different countries. In fact, it was concluded by the EC that prices were 80% higher in Belgium than in Ireland and 138% higher in Denmark than in Ireland. Nevertheless, as argued by Bishop and Walker¹⁵⁴, a policy by a dominant undertaking of pricing differently across countries does not necessarily imply consumer harm and therefore does not necessarily represent abusive behaviour.

215. In a nutshell, the OFC opines that it is important to carry out several comparisons in order to gather sufficiently reliable evidence that the disputed price is significantly and persistently above the normal competitive price. As outlined in Article 9(3) of the Competition Act, in order to determine whether the purchase or selling price is excessive or unfair, one needs to consider all relevant factors, in particular:

- a. the price charged for the product (in absolute terms);
- b. the percentage increase or increases in the price over the long and short term;
- c. the relationship between the price and the cost of the product;
- d. the period of time for which the price has been charged;
- e. the economic value of the product;
- f. the importance of the product to consumers;
- g. the economic or other risks associated with bringing the product to the market;
- h. the investment of capital and other resources necessary to bring the product to the market;
- i. the expected, probable or possible changes in the market for the product; and
- j. the price charged for the product by other undertakings in Malta and by the same or other undertakings in other analogous markets.

Taking the above factors into consideration limits the likelihood of the OFC committing a Type One Error, i.e. when it is concluded that prices are excessive when in reality, they are competitive or a Type Two Error i.e. conclusion that prices are competitive when in reality they are not.

216. In order to determine excessive pricing, there must be a significant and persistent difference between the disputed price and the price that would be expected in a competitive market¹⁵⁵.

¹⁵¹ Case C-177/16 EU:C:2017:689.

¹⁵² *Ibid*, paragraph 38.

¹⁵³ *Ibid*, paragraph 56.

¹⁵⁴ Bishop and Walker, 2010. *The Economics of EC Competition Law: Concepts, Application and Measurement*. University Edition., Sweet & Maxwell.

¹⁵⁵ *Ibid*, paragraph 55.

C. Assessment of Abuse of Dominance via Excessive Pricing

217. The first stage of the *United Brands* test requires an assessment of whether the prices charged by MDP for each product is excessive when compared to their Cost Plus which is composed of:
- a. The costs incurred by MDP in respect of their products composed of both the direct costs and an appropriate apportionment of indirect costs.
 - b. A reasonable rate of return for each product.
218. Once these are established, it is then necessary to assess whether and, if so, by what amount the prices charged exceed Cost Plus. If a price exceeds Cost Plus, consideration then needs to be given as to whether the difference between the price charged and the Cost Plus, hereinafter referred to as the 'excess', is '*material*' and '*sufficiently large to be deemed excessive*' for the purposes of the *United Brands* test.

a. Assessment of the Prices charged, and the Costs incurred by MDP – United Brands Test

219. The OFC has relied on the data it has obtained from MDP during the course of the investigation in order to assess whether its prices are excessive. The data obtained from MDP spans the period 2012-2019. Although the OFC has analysed the data in its entirety, for the purposes of this report, only data for 2019 attributed to pre- and post-price increases is illustrated unless otherwise mandated by case law.

I. MDP's Prices

220. The final consumer price of fresh milk products is not set by MDP but is set at the discretion of the retailers. MDP issues to distributors a price list for its products together with a RWP (the recommended prices at which MDP recommends that the distributor sells to its customers) and a RCP (the recommended price at which MDP recommends that its products are sold to the final consumer). The RWP is non-binding on the distributor, and the distributor is free to sell to its customers at any price. Similarly, the RCP is non-binding on the retailer, and the retailer is free to sell to its customers at any price.
221. While MDP also services direct customers that are retailers, the majority of MDP's point of sale comes about when the dairy products are sold to the distributors. As a result, the OFC will assess the costs actually incurred by MDP in supplying the products and make a comparison with the prices actually charged to the distributors.
222. At the request of the OFC, MDP has provided the pre- and post-price increases of the selling price to distributors and the RCP for the focal product. The changes in both prices are illustrated in tables 13 and 14, respectively.
223. As highlighted in tables 13 and 14, the difference between the old and the new selling price to distributors and the old and the new RCP means that without making a distinction between the profits retained by the distributors as compared to those retained by the retailers, collectively they can enjoy higher mark-ups post price increases.

Table 13: MDP's Selling Price to Distributors

	Old Selling Price to Distributors (€)	New Selling Price to Distributors (€)	Increase (€)	Increase (%)
Whole Milk 1L	[✂]	[✂]	[✂]	[✂]
2.5% Fat Milk 1L	[✂]	[✂]	[✂]	[✂]
Skimmed Milk 1L	[✂]	[✂]	[✂]	[✂]
Lactose Free Milk 1L	[✂]	[✂]	[✂]	[✂]
Whole Milk ½ L	[✂]	[✂]	[✂]	[✂]
2.5% Fat Milk ½ L	[✂]	[✂]	[✂]	[✂]
Skimmed Milk ½ L	[✂]	[✂]	[✂]	[✂]
Lactose Free Milk ½ L	[✂]	[✂]	[✂]	[✂]

Source: MDP submissions, dated 2 September 2019.

Table 14: MDP's RCP Increases

	Old Recommended Consumer Price (€)	New Recommended Consumer Price (€)	Increase (€)	Increase (%)
Whole Milk 1L	0.86	0.96	0.10	11.63
2.5% Fat Milk 1L	0.83	0.94	0.11	13.25
Skimmed Milk 1L	0.81	0.92	0.11	13.58
Lactose Free Milk 1L	1.10	1.15	0.05	4.55
Whole Milk ½ L	0.49	0.56	0.07	14.29
2.5% Fat Milk ½ L	0.47	0.54	0.07	14.89
Skimmed Milk ½ L	0.46	0.52	0.06	13.04
Lactose Free Milk ½ L	0.63	0.65	0.02	3.17

Source: MDP submissions, dated 2 September 2019; Author's Calculations.

II. MDP's Costs and Profitability

224. At the request of the OFC, MDP has provided a breakdown of the relevant total costs of production at product level.

225. MDP was registering a loss in its largest market segment which is the fresh milk category. As highlighted in table 15, this clearly affected the operating profits of the company in 2018.

226. Furthermore, it was also noted that in June 2019, MDP rationalized its pricing structure in order to sustain raw milk output in light of revised costing calculations at farm level. This resulted in an increase in the price of raw milk which further exacerbated the loss per unit of fresh milk sold.

227. The tables below establish the total cost per unit of each fresh milk product under investigation. The costings of 2019 are produced hereunder at three stages namely as at 1 January, 2019 (pre price increases), as at 1 June, 2019 (pre price increases but immediately after the latest raw milk price increase) and as at 29 July, 2019 (post price increases).

Table 15: Costings as at January 1, 2019

	Whole Milk 1L	2.5% Fat Milk 1L	Skimmed Milk 1L	Lactose Free Milk 1L	Whole Milk ½ L	2.5% Fat Milk ½ L	Skimmed Milk ½ L	Lactose Free Milk ½ L
	€/unit	€/unit	€/unit	€/unit	€/unit	€/unit	€/unit	€/unit
Selling Price to Distributors	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Returns	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Raw Materials	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Direct Labour	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Packaging Costs	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Gross Profit	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Indirect O'Heads	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Net Profit	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Mark Up (%)	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]

Source: MDP submissions, dated 12 September 2019.

Table 16: Costings as at June 1, 2019

	Whole Milk 1L	2.5% Fat Milk 1L	Skimmed Milk 1L	Lactose Free Milk 1L	Whole Milk ½ L	2.5% Fat Milk ½ L	Skimmed Milk ½ L	Lactose Free Milk ½ L
	€/unit	€/unit	€/unit	€/unit	€/unit	€/unit	€/unit	€/unit
Selling Price to Distributors	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Returns	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Raw Materials	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Direct Labour	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Packaging Costs	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Gross Profit	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Indirect O'Heads	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Net Profit	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Mark Up (%)	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]

Source: MDP submissions, dated 12 September 2019.

Table 17: Costings as at 29 July, 2019

	Whole Milk 1L	2.5% Fat Milk 1L	Skimmed Milk 1L	Lactose Free Milk 1L	Whole Milk ½ L	2.5% Fat Milk ½ L	Skimmed Milk ½ L	Lactose Free Milk ½ L
	€/unit	€/unit	€/unit	€/unit	€/unit	€/unit	€/unit	€/unit
Selling Price to Distributors	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Returns	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Raw Materials	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Direct Labour	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Packaging Costs	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Gross Profit	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Indirect O'Heads	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Net Profit	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Mark Up (%)	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]

Source: MDP submissions, dated 12 September 2019.

228. Raw materials reflect the cost of raw milk supplied daily by the local herdsman. MDP accepts a limited amount of returns due to manufacturing defects and unsold fresh products that clients (mainly large ones) are caught with. On the other hand, the labour costs are the costs incurred to supply the final product while the packaging costs mainly reflect the cost of the milk carton and the light cap. The indirect overheads are reflecting an absorption of administration and selling expended per unit.

229. Given that more than four-fifths of the direct costs incurred are attributed to raw materials, the OFC felt the need to analyse this cost component in more detail.

Raw Materials

230. According to submissions made by MDP, since the last price hike in fresh milk products which was in August 2012, the price paid for raw milk fluctuated considerably. There are mainly three factors which have affected the price for raw milk: (i) changes in the international prices of cereals, (ii) Cost-of-Living Adjustments, and (iii) the rationalisation of the pricing structure.

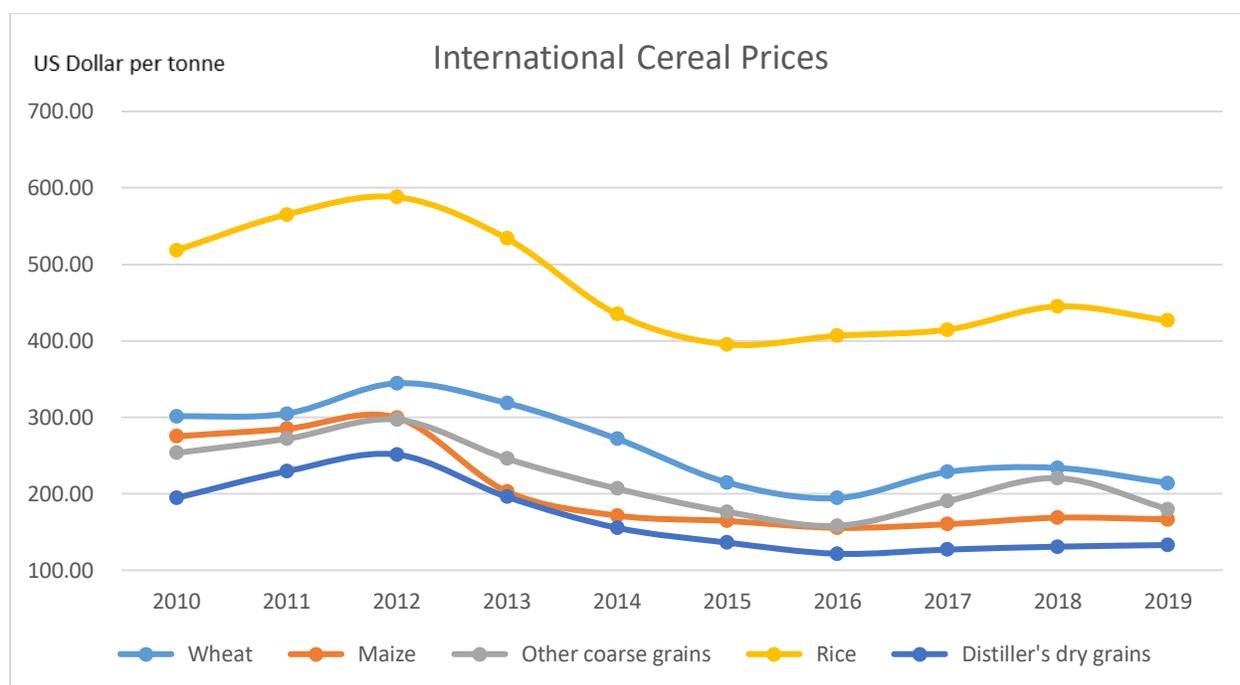
a. International Prices of Cereals

231. The period 2010-2012 was characterised by an international increase in the price of cereals in the face of diminishing world stocks available. A turnaround was seen in subsequent periods as successive record harvests of major cereals have led to a significant build-up of inventories and low prices on international markets. Figure 9 depicts the international prices of cereals.

232. Maize (also known as corn) is generally categorised into one of two broad groups: yellow and white. Yellow maize accounts for the bulk of the total world maize market and is predominantly used for animal feed¹⁵⁶. As a result, the time-series analysis of cereal prices is devoted to this commodity.

233. The successes achieved during the 2013-2016 period in terms of world production have led to declines in cereal prices. In fact, maize has seen its price declining by an average of 14.3% during the above-mentioned period. Yet, subsequent periods were again characterised by a gradual destocking of maize, leading its price to increase by 3.0% and by 5.3% in 2017 and 2018, respectively. A marginal decrease of 1.3% was recorded in world maize prices in 2019, partly attributed to a base effect when compared to the previous period.

Figure 9: International Cereal Prices



Source: OECD-FAO Agricultural Outlook 2020-2029. Data accessed on 15 September, 2020.

b. Cost-of-Living Adjustment

234. The cost-of-living adjustment is an amount of money adjusted yearly to protect and maintain a certain standard of living. These adjustments are based on the Retail Price Index, an

¹⁵⁶ OECD's website, accessed 15 September 2020, < <https://www.oecd-ilibrary.org/sites/57d27093-en/index.html?itemId=/content/component/57d27093-en>>.

economic indicator that measures inflation in Malta. In Malta, the cost of living adjustment is announced during the national budget speech and comes into effect in January of the following year.

c. Rationalised Pricing Structure to sustain Raw Milk Output

235. MDP purchases raw milk from KPH members on the basis of contracts between MDP and individual milk producers. A contract sets an annual milk volume, specific to the individual contract, which MDP purchases from the producer according to a pricing scheme that is applicable to all producers. Individual producers can furthermore sell raw milk to MDP in excess of the contract volume, at prices established by MDP and which are equally applicable to all producers.¹⁵⁷

236. In July 2019, the method for the establishment of the price applicable to the individual contract milk volume was reviewed as to:

- i. Encourage producers to increase their supply of milk especially in the summer through / low supply period. In the summer of 2018, MDP faced a shortage of supply of milk from milk producers leading to shortages of products on the local market. This caused MDP irreparable harm in lost sales and customer dissatisfaction. The new milk price mechanism stimulates growth by giving a better price for raw milk the higher a producer goes in supplying to the company the contractually agreed volume. The price for raw milk at [%] fat and [%] protein is of [%]/ litre for the first 50% of supply and increases to [%]/ litre for the next 25% and to [%]/ litre for the last quarter. Moreover, in the summer months, the price of the last quarter increases to [%]/ litre. Moreover, any volume of raw milk supplied which is above the contractual annual milk volume but under the specified capping is paid at [%]/ litre in winter and [%]/ litre in summer while when exceeding the capping, the price per litre declines to [%] in winter but remains at par in summer.
- ii. Sustain a policy of growth in the dairy sector.
- iii. Give a fair price for raw milk to milk producers that will encourage them to remain working on their farms within the local milk industry. This is an extremely important issue that is being taken seriously by MDP given that the number of farmers is always decreasing, and the average age of registered milk producers in Malta is well over 50 years.
- iv. Give greater stability to milk producers through a simpler and more straightforward system, thus enabling the milk producer to better plan his milk supply over a period of time.
- v. Put the milk sector in Malta on a more sustainable path.¹⁵⁸

237. This scheme presumes that 100% of the contract amount reflects the operating scale of the farm. The price of raw milk offered on that amount, at an average of [%]/ litre and subject to an increasing scale as an incentive to achieve the scale production volume is intended for an

¹⁵⁷ Source: MDP submissions, dated 19 November 2019.

¹⁵⁸ Source: MDP submissions, dated 2 September 2019.

efficiently operating farm to recover its average total costs inclusive of normal operating profit. The price at an average of [€]/ litre of raw milk offered on the band of volume above the scale amount is intended to reflect the recovery of marginal costs of extending production beyond the scale level, and an element of profit which incentivises output growth in line with the requirements of MDP. Levels of output (in the winter months) that are beyond this attract a price of only [€]/ litre of raw milk, as these are for the foreseeable future considered to go beyond the requirements of MDP.

238. The establishment of the efficient level of average total cost of raw milk production in Malta is based on a benchmarking exercise of costs of raw milk production in foreign jurisdictions. Relevant data is indicated in table 18, which relates to EU averages from six countries.¹⁵⁹

Table 18: Cost of Raw Milk Production in Foreign Jurisdictions

	EU average (€ / litre)	Range (Max-Min)	% of total cost
Input Costs	0.176	0.038	35%
General Operating Costs	0.216	0.094	42%
Labour Costs	0.117	0.135	23%
Subsidies	-0.036	0.053	-7%
Return on Investment	-0.036	0.043	7%
Total	0.509	0.071	100%

239. The average cost across the sample of EU countries considered is derived at €0.509, with a range of €0.071.

240. The comparable figures obtained from an internal study conducted by MDP based on a sample of 60 farms in Malta and Gozo are as follows:

¹⁵⁹ Source: 2017 report titled “What is the Cost of Producing Milk?”, issued by the European Milk Board. The countries covered are Belgium, Denmark, France, Netherlands and Luxembourg; MDP submissions, dated 19 November 2019.

Table 19: Cost of Raw Milk Production in Malta and EU average

	EU average (€ / litre)	Malta (€ / litre)	Difference (MT – EU)
Input Costs	0.176	[REDACTED]	[REDACTED]
General Operating Costs	0.216	[REDACTED]	[REDACTED]
Labour Costs	0.117	[REDACTED]	[REDACTED]
Subsidies	-0.036	[REDACTED]	[REDACTED]
Return on Investment	0.036	[REDACTED]	[REDACTED]
Total	0.509	[REDACTED]	[REDACTED]

Source: MDP submissions, dated 19 November 2019; Author's Calculations.

241. The average cost of raw milk production in Malta, at [REDACTED] per litre, is higher than the EU average of €0.509 per litre.¹⁶⁰ In terms of costs composition, input costs consisting mainly of feed¹⁶¹ is the predominant element in Malta, which is significantly higher than the EU average. This reflects the lack of grazing resources and Malta's dependence on imported feed in the context of a small and peripheral markets which tend to inflate costs. There are also significant variations in this cost component among farms in Malta, reflecting different practices and efficiency attainments. On the other hand, farm operating and labour costs in Malta are significantly less than those in the EU, as is the return on investment¹⁶².

242. Hence, MDP opines that on the basis of the above analysis, it considers the average price on the contract volume of [REDACTED]/ litre sufficient to sustain the efficient production of raw milk in Malta. It is a price that is also consistent with cost performance in raw milk production across the EU.¹⁶³

243. On the other hand, the marginal cost of raw milk production in excess of the contract volume is dependent on two incremental factors:

- i. The cost of acquisition or rearing of an animal at the point where it is ready to start producing milk;
- ii. the direct cost of feed.

The other costs are not considered to be incremental in this regard.¹⁶⁴

244. The direct cost of feed across a sample of 60 farms is found to be in the range of [REDACTED] to [REDACTED] per litre of milk produced, with a midpoint of [REDACTED]. The cost to acquire an animal at the point that it is ready to commence production is currently [REDACTED]. Over an estimated lifetime production of

¹⁶⁰ Not included in these figures are the revenues from associated beef production, which stands at €0.027 per kilogram of milk in Malta as compared to €0.052 per kilogram of milk in the EU. Source: MDP submissions, dated 19 November 2019.

¹⁶¹ As well as direct utility costs, consisting of around €0.03 per kilogram of milk. Source: MDP submissions, dated 19 November 2019.

¹⁶² Source: MDP submissions, dated 19 November 2019.

¹⁶³ Ibid.

¹⁶⁴ Ibid.

[€] litres of raw milk, this entails a cost per litre of milk of [€]. Therefore, a price of [€] per litre of raw milk is considered to be proportionate to the requirement.¹⁶⁵

245. For the reasons mentioned above, mainly due to price of feeds increases, Malta's raw milk price ranks among the highest prices for dairy farmers in the EU. This is to be expected given Malta's reliance on feed imports as well as the natural and structural disadvantages of the local dairy sector. It is noteworthy that the price of raw milk is lower when compared to the price of raw milk in the island of Cyprus where the dairy sector resembles the same characteristics as that of Malta.¹⁶⁶¹⁶⁷

246. Over recent years, the above three factors have all contributed to varying degrees and explain the current price of [€] that MDP pays to local herdsmen for every litre of raw milk produced. Table 20 outlines the main changes in raw milk prices that occurred between 2010 and mid-2019.

247. MDP stresses that the increase in the cost of raw milk emanating from the rationalising of the pricing structure is considered to be an investment in the local milk sector and is viewed crucial to ensure the long-term survival of this important sector.¹⁶⁸

248. The OFC agrees with the rationalisation of the pricing structure implemented by MDP. The OFC opines that this provides adequate compensation to local herdsmen given the unique local circumstances.

¹⁶⁵ Source: MDP submissions, dated 19 November 2019.

¹⁶⁶ P. Von Brockdorff and G. Buttigieg (2015), *Sectoral Impact: An Insight into How the Maltese Dairy Sector Adapted to EU Membership*, Reflection on a Decade of EU Membership, Occasional Paper 06/2015.

¹⁶⁷ Source: Statistics by the European Commission: EU Prices of Cow's Raw Milk in Euro / 100kg, accessed 16 September 2020, <https://ec.europa.eu/info/sites/info/files/food-farming-fisheries/farming/documents/eu-raw-milk-prices_en.pdf>.

¹⁶⁸ Source: MDP submissions, dated 2 September 2019.

Table 20: Raw Milk Price Table 2010-2019 (for milk at [redacted]% fat and [redacted]% protein)

Effective Date	Reason for Change	Price / Litre
01.01.2010	COLA	[redacted]
14.10.2010	Change in International Cereal Prices	[redacted]
01.01.2011	COLA	[redacted]
22.02.2011	Change in International Cereal Prices	[redacted]
07.03.2011	Change in International Cereal Prices	[redacted]
01.01.2012	COLA	[redacted]
09.01.2012	Change in International Cereal Prices	[redacted]
04.06.2012	Change in International Cereal Prices	[redacted]
12.09.2012	Change in International Cereal Prices	[redacted]
06.12.2012	Change in International Cereal Prices	[redacted]
01.01.2013	COLA	[redacted]
04.04.2013	Change in International Cereal Prices	[redacted]
13.08.2013	Change in International Cereal Prices	[redacted]
15.11.2013	Change in International Cereal Prices	[redacted]
01.01.2014	COLA	[redacted]
21.10.2014	Change in International Cereal Prices	[redacted]
01.01.2015	COLA	[redacted]
01.01.2016	COLA	[redacted]
05.02.2016	Change in International Cereal Prices	[redacted]
01.01.2017	COLA	[redacted]
16.01.2017	Change in International Cereal Prices	[redacted]
01.01.2018	COLA	[redacted]
03.05.2018	Change in International Cereal Prices	[redacted]
01.01.2019	COLA	[redacted]
01.06.2019	Rationalised Pricing structure to sustain raw milk output in the light of revised costing calculations at farm level	[redacted]

Source: MDP submissions, dated 12 September 2019.

III. Reasonable Rate of Return

249. Having estimated the total costs incurred, the OFC must establish the 'Plus' element of Cost Plus that is, a reasonable rate of return.¹⁶⁹ In order to establish the Plus element, according to the CMA, it is necessary to determine: first, what is the most appropriate measure of return to use; and second, what would be a reasonable rate using that measure.¹⁷⁰
250. The OFC considered three possible measures for MDP's rate of return, namely: ROCE, ROS and gross margins. A brief description of each measure is provided hereunder:
- a. ROCE is defined as total assets less current liabilities or fixed assets plus working capital. It measures profits against the capital employed to produce them. This measure is widely renowned and accepted in the business industry. The main problem usually encountered is the difficulty to measure capital employed. The standard approach would be to use balance sheet values. However, this can give rise to three main problems: (i) asset values may be historical and therefore may not be an accurate reflection of current values; (ii) asset values may be inflated to reflect any excess profit they are able to generate and therefore a return based on that value would allow the business an excessive return; and (iii) the economic activity of the undertaking may not be separately recorded on the balance sheet or not completely recorded – the problem of cost identification.¹⁷¹
 - b. ROS is a measure of the return on sales after the deduction of both direct and indirect costs. ROS is a straightforward measure of profit. However, this measure is limited when it comes to investigating excessive pricing as it would not be appropriate to calculate the reasonable ROS allowance based on actual revenue generated from prevailing prices. Instead, a reasonable ROS should be calculated through an uplift on costs.¹⁷²
 - c. Gross margin is defined as the difference between revenue and costs of goods sold. Gross margin is a common measure of profitability as it can be easily calculated. However, it is not a complete measure as it fails to take into account all of the support activities which may be essential to achieve sales. It is generally used where ROS cannot be calculated with sufficient accuracy due to the difficulty in allocating indirect costs.¹⁷³
251. ROCE would be the OFC's preferred measure of return as it is a well-known profitability measure which assesses profits against the capital employed. However, given that MDP manufactures other products than fresh milk, it is somehow difficult to allocate the proportion of capital assets used to produce fresh milk with precision.

¹⁶⁹ Albion Water II, paragraph 89; Attheraces Ltd v British Horseracing Board Ltd [2007] EWCA Civ 38; [2007] UKCLR 309, CA, paragraph 209;

¹⁷⁰ Decision of the Competition and Markets Authority. Unfair Pricing in respect of the supply of phenytoin sodium capsules in the UK. Case CE/9742-13, 7 December 2016.

It is noteworthy that although the CAT's judgement was upheld, the Court of Appeal did not uphold the CATs' approach in its entirety. Indeed, it agreed with the CMA that it was entitled to take a cost plus approach to determine whether the prices in question were excessive so as to amount to an abuse of a dominant position.

¹⁷¹ Ibid.

¹⁷² Ibid.

¹⁷³ Ibid.

252. Similarly, given that the OFC can identify and allocate MDP's indirect costs to fresh milk products, the OFC opines that gross margin is an incomplete and less informative measure than ROS and therefore not a suitable measure of rate of return in this case. On the other hand, ROS is also limited when it comes to investigating excessive pricing.

253. Determining what a reasonable rate of return should be is an exercise of judgement and depends on the specific facts of each case.¹⁷⁴

254. For these reasons, the OFC decided to base its judgment of a 'reasonable rate of return' based on a hybrid approach which involves both the ROCE and the ROS measure. This would also help the OFC to cross-check its results and gauge the sensitivity of results when employing different indicators.

255. Based on its audited accounts, MDP submitted that between the period 2014 – 2018, it registered the following ROCE and ROS:

Table 21: MDP's ROCE and ROS for the period 2014 - 2018

	2014	2015	2016	2017	2018
Operating Profit / (Loss)	[X]	[X]	[X]	[X]	[X]
Earnings before Interest and Tax (EBIT)	[X]	[X]	[X]	[X]	[X]
Gross Profit	[X]	[X]	[X]	[X]	[X]
Sales	[X]	[X]	[X]	[X]	[X]
[Total Assets – Current Liabilities]	[X]	[X]	[X]	[X]	[X]
ROCE (%)	10.01%	11.11%	7.67%	4.44%	-3.41%
ROS (%)	5.18%	6.95%	4.78%	2.70%	-2.60%

Source: MDP submissions, dated 19 November 2019.

256. The OFC considered whether there are any benchmarks which may indicate what would be a reasonable rate of return for the calculation of Cost Plus for MDP's products. Given that MDP is the only processing dairy plant in Malta producing fresh milk products, the OFC could not refer to an industry benchmark to determine a reasonable rate of return for manufacturing fresh milk. Notwithstanding this, the OFC considered MDP's audited figures and the ROCE and ROS of other manufacturers operating within the primary sector and having similar size as that of MDP.

257. In considering the relevance of these benchmarks as to what might be a reasonable rate of return for the calculation of Cost Plus for MDP's fresh milk products, the OFC took into account the importance of the product to consumers, the economic and other risks associated with bringing the product to the market and the investment of capital and other resources necessary to bring the product to the market.

¹⁷⁴ Decision of the Competition and Markets Authority. Unfair Pricing in respect of the supply of phenytoin sodium capsules in the UK. Case CE/9742-13, 7 December 2016, paragraph 5.85.

258. As highlighted in table 21, over the period 2014 to 2018, MDP has registered an operating loss in 2018 and an operating profit in the remaining years. Notwithstanding operating at a profit and despite MDP having a dominant position in the market, MDP operated at very low mark-ups. In fact, the average profit/sales ratio over the period 2014 to 2018 stood at 3.4%, which is considered to be very low by corporate standards. In terms of return on sales, 2015 is considered to be the best year, with a ROS of nearly 7.0%.

259. The same remarks could also be made when looking at the ROCE. In fact, as can be seen from the same table, over the period 2014 to 2018, the average ROCE stood at nearly 6.0% which is considered to be low by corporate standards. It is also worth noting that in 2012 and 2013, MDP operated at a loss. Over the period under review, the highest ROCE of 11.1% was achieved in 2015.

260. It is widely accepted that in general, companies are happy with a ROS ranging between 5-10%. In fact, when comparing ROS indicators of state-owned enterprises and private companies, Kwiatkowski et al. (2015) noted that the ROS for state-owned enterprises equals 7.4% when compared to 6.6% for private companies while in the period 2008-2011 characterised by a global financial recession, the average ROS for private companies was 4.6% while that for state-owned enterprises was 3.6%. As a result, it is evident that according to Kwiatkowski et al. (2015), state-owned enterprises in the period characterised by the global financial recession and the subsequent recovery recorded a higher ROS than that registered by MDP over the period 2014-2018. Furthermore, a ROCE of 10% is considered to be the long-term average for the wider market.¹⁷⁵ It is important to note that these figures vary between industries and sectors and also between firms with different sizes and maturity levels.

261. The OFC opines that the closest local manufacturer operating within the primary sector with a similar size as that of MDP is Magro Brothers.¹⁷⁶ Based on audited accounts, the ROS and ROCE of Magro Brothers Group of Companies for the 2014 – 2019 period stood as follows:

Table 22: Magro Brothers Group of Companies ROCE and ROS for the period 2014 - 2019

	2014	2015	2016	2017	2018	2019
ROCE (%)	2.0%	3.4%	3.3%	2.8%	2.5%	-0.8%
ROS (%)	2.6%	3.9%	4.7%	4.1%	3.7%	-1.2%

Source: Audited Accounts; Author's Calculations.

262. As highlighted in table 22, over the period 2014 to 2019, Magro Brothers Group of Companies registered an average ROCE of 2.2% and an average ROS of 3.0%, which are considered to be very low by international standards.

263. The OFC opines that the weak and negative financial position recorded by MDP in 2017 and 2018 compromise MDP's presence in the local market. The OFC is also of the opinion that with the recorded ROCE and ROS figures in 2017 and 2018, it would be highly unlikely for the

¹⁷⁵ Source: MoneyWeek press release, accessed 17 September 2020, <<https://moneyweek.com/glossary/return-on-capital-employed-roce>>.

¹⁷⁶ The Magro Brothers Group of Companies is a family owned organisation dedicated to the production and provision of quality lzfood. Source: Magro Brothers Group of Companies Website, accessed 05 October 2020, <<https://www.magro.com.mt/>>.

company to undertake the envisaged investment programme¹⁷⁷ that is necessary to continue sustained operations in the future.

264. Taking the above into account, alongside with the economic value and the importance of the product to consumers, the OFC opines that a ROS of 5% (the lowest threshold considered decent for companies to operate) is an appropriate reasonable rate of return. Similarly, the OFC is of the opinion that a ROCE of 7% is an appropriate reasonable rate of return on capital employed under such circumstances.

IV. Calculation of the reasonable rate of return and Cost Plus

265. Having assessed the reasonable rate of return under each measure, this section sets out the results of the calculation of the reasonable rate of return and the resultant cost plus for MDP's fresh milk products.

i. ROS

266. Using a ROS figure of 5%, Table 23 below sets out the allowance for a reasonable return and the resultant cost plus figures for each of MDP's fresh milk products on a per item basis. Table 24 below sets out the equivalent allowance and cost plus figures for each of MDP's fresh milk products on a revenue basis, taking 2018 volume sales figures.

¹⁷⁷ The company will be making an investment in new dairy and ancillary operation totalling €49.0 million. The investment is expected to improve quality and production efficiencies through application of latest technologies. It will facilitate introduction of new dairy products on the market by introducing feasible short production runs and will enable the company to meet, efficiently and economically, every increasing environmental and HACCP quality standards. Source: MDP submissions, dated 19 November 2019.

Table 23: MDP’s allowances for a reasonable rate of return and the resultant Cost Plus figures for each of MDP’s products, using a ROS of 5%, on a per item basis.

	Whole Milk 1L	2.5% Fat Milk 1L	Skimmed Milk 1L	Lactose Free Milk 1L	Whole Milk ½ L	2.5% Fat Milk ½ L	Skimmed Milk ½ L	Lactose Free Milk ½ L
	€/unit	€/unit	€/unit	€/unit	€/unit	€/unit	€/unit	€/unit
Selling Price to Distributors	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Direct Costs	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Indirect Costs	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Allowance for reasonable return	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Cost Plus	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Difference between Selling Price and Cost Plus	-0.0091	-0.0272	-0.0387	0.0229	0.0368	0.0206	0.0063	0.0439

Source: MDP submissions, dated 12 September 2019; Author’s Calculations.

Table 24: MDP’s allowances for a reasonable rate of return and the resultant Cost Plus figures for each of MDP’s products, using a ROS of 5%, on a revenue basis.

	Whole Milk 1L	2.5% Fat Milk 1L	Skimmed Milk 1L	Lactose Free Milk 1L	Whole Milk ½ L	2.5% Fat Milk ½ L	Skimmed Milk ½ L	Lactose Free Milk ½ L
	€	€	€	€	€	€	€	€
Revenues	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Total Direct Costs	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Total Indirect Costs	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Allowance for reasonable return	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Cost Plus	[X]	[X]	[X]	[X]	[X]	[X]	[X]	[X]
Difference between Revenues and Cost Plus	(31,645)	(347,670)	(244,200)	22,997	2,670	44,578	13,601	5,451

Source: MDP submissions, dated 12 September 2019; Author’s Calculations.

iii. ROCE

267. In order to cross-check that the OFC’s assessment of MDP’s allowance for a reasonable return on a ROS basis is appropriate, the OFC has also calculated an allowance for a reasonable return on a ROCE basis. Using this approach, it is first necessary to estimate the capital employed by MDP in producing and supplying MDP’s fresh milk products.

268. The OFC refers to MDP’s submissions dated 19 November 2019 whereby the following data illustrated in Table 25 was provided:

Table 25: MDP's ROCE and ROS for the period 2014 - 2018

	2014	2015	2016	2017	2018
Operating Profit / (Loss)	[✂]	[✂]	[✂]	[✂]	[✂]
Earnings before Interest and Tax (EBIT)	[✂]	[✂]	[✂]	[✂]	[✂]
Gross Profit	[✂]	[✂]	[✂]	[✂]	[✂]
Sales	[✂]	[✂]	[✂]	[✂]	[✂]
[Total Assets – Current Liabilities]	[✂]	[✂]	[✂]	[✂]	[✂]
ROCE (%)	10.01%	11.11%	7.67%	4.44%	-3.41%
ROS (%)	5.18%	6.95%	4.78%	2.70%	-2.60%

Source: MDP submissions, dated 19 November 2019.

269. Table 26 sets out Cost Plus for MDP's fresh milk products using a ROCE of 7%. In its calculations, the OFC is assuming the same capital employed as that recorded for 2018 and apportioned on each fresh milk product category based on 2018 sales volume data.

Table 26: MDP's allowances for a reasonable rate of return, using a ROCE of 7%, and the resultant Cost Plus figures for each of MDP's products.

	Whole Milk 1L	2.5% Fat Milk 1L	Skimmed Milk 1L	Lactose Free Milk 1L	Whole Milk ½ L	2.5% Fat Milk ½ L	Skimmed Milk ½ L	Lactose Free Milk ½ L
	€	€	€	€	€	€	€	€
Revenues	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Total Direct Costs	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Total Indirect Costs	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Allowance for reasonable return	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Cost Plus	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Difference between Revenues and Cost Plus	-64,288	-479,123	-313,410	17,613	719	-15,355	-47,748	2,301

Source: MDP submissions, dated 12 September 2019; Author's Calculations.

270. The OFC considers that these results further support the OFC's assessment and analysis based on a ROS of 5%.

V. Conclusion on whether MDP's Prices are excessive

271. Based on the above calculations, the OFC concludes that the excesses set out in tables 23, 24 and 26 are definitely not '*material*' and '*sufficiently large to deemed excessive*' in the context of the *United Brands Test*. Furthermore, as argued in *Attheraces*, the UK Court of Appeal said that evidence that a firm was pricing above cost did not provide sufficient evidence to conclude that prices were excessive: above cost pricing was held to be a necessary but not a sufficient condition for excessive pricing.¹⁷⁸

272. This conclusion is further corroborated by the fact that, while they are not determinative, the OFC has referred to the magnitude of the excesses that have been found to be excessive in other cases as highlighted in paragraph 202 of this decision.

273. This conclusion is further supported by the fact that when summing up the difference between the revenues and cost plus based on both the ROS and ROCE on a revenue basis, the aggregate resultant is negative indicating that post selling price increases, MDP is expecting a ROCE and ROS which are lower than the reasonable rates of return identified by the OFC.

274. As stated by the Court of Justice in *United Brands*, the United Brands test consists of a cumulative two-stage test whereby the second limb is only studied after finding evidence that the '*difference between the costs actually incurred and the price actually charged is excessive*'.¹⁷⁹ Consequently, provided that the first limb of the United Brands test has not been satisfied, the OFC opines that an assessment of the second limb of the United Brands test is not necessary.

b. Assessment of Abuse of Dominance via Excessive Pricing – Other important Considerations

275. As argued by De Coninck (2018), the *United Brands* test on its own is insufficient to establish an abuse, as while it provides insights for determining whether prices are excessive (i.e. is the price excessive in relation to cost, and if in the affirmative, can it be objectively justified?), it fails to provide sufficient conditions for establishing an abuse.

276. Following *United Brands*, the European Commission and national competition authorities have been reluctant to pursue exploitative cases. To a certain extent, this is economically justified. As argued by De Coninck (2018), there is generally little reason, from a welfare point of view, for a competition authority to pursue excessive pricing cases; "*high prices are necessary to reward investment, and act as a signal to attract further investment and entry. Limiting dominant firms' ability to extract the market power that they have lawfully obtained through their past investment, risk taking and business acumen would thus stifle investment and innovation, which would be economically inefficient*".

¹⁷⁸ *Attheraces Ltd v British Horseracing Board Ltd* [2007] EWCA Civ 38; [2007] UKCLR 309, CA.

¹⁷⁹ *United Brands v Commission*. Case 27/76. Court of Justice, [1978] 1 CMLR 429, paragraph 252.

277. Yet, the rare exceptions concerning case law on excessive pricing typically concern abuses of both exploitative and exclusionary conduct and regulated industries. As explained by Advocate General Wahl, “...in its practice, the Commission has been extremely reluctant to make use of that provision against (allegedly) high prices practiced by dominant undertakings. Rightly so, in my view. In particular, there is simply no need to apply that provision in a free and competitive market: with no barriers to entry, high prices should normally attract new entrants. The market would accordingly self-correct. It may however be different in markets with legal barriers to entry or expansion and, in particular, in those in which there is a legal monopoly. Indeed, there may be markets which, because of their particular features, are not run efficiently when open to competition.”¹⁸⁰
278. De Coninck further argues that intervention for excessive prices, even if the *United Brands* test is passed, would arguably require specific market conditions to be justified.
279. The case law referred to earlier in this chapter shows that the European Commission and European Courts addressed the question of excessive prices only in markets with an entrenched dominant position where entry and expansion of competitors could not be expected to ensure effective competition in the foreseeable future. For example, in *General Motors*¹⁸¹ and *Deutsche Post*¹⁸², there was the presence of a legal monopoly, *SACEM*¹⁸³ was characterised by a national monopoly based on network effects, in *Bodson*¹⁸⁴, the dominant position was based on an accumulation of exclusive concessions which shielded a sizeable part of the market from competition, a natural monopoly characterised *Helsingborg*¹⁸⁵ while in *Rambus*, a dominant position based on a lock-in effect through industry standard was present. The only exception was *United Brands*.¹⁸⁶¹⁸⁷
280. The OFC opines that at a national level, MDP enjoys the characteristics of a natural monopoly with high and long-lasting barriers to entry and expansion. This opinion is supported by the fact that it has established network effects and lock-in effects with local herdsman and network effects with distributors and retailers. As a result, while there is scope for potential competition in the focal product, this is highly unlikely to be exerted by a local manufacturer but is likely to be ensued by an importer importing foreign fresh milk products.
281. On the other hand, the OFC agrees with the arguments put forward by De Coninck and by Advocate General Wahl in the sense that one would need to earn a reasonable rate of return in order to pursue ambitious investment programmes. As a result, the OFC is aware of the trade-off

¹⁸⁰ Opinion of Advocate General Wahl, delivered on 6 April 2017, following a request for a preliminary ruling by the Latvian Supreme Court on the conditions under which the rates set by the Latvian collecting society AKKA/LAA are excessive under Article 102 (hereafter, “AG Wahl’s Opinion of 6 April 2017”). See Tim Kasten, EU Court of Justice Advocate General Wahl offers guidance on the criteria to identify excessive prices in abuse of dominance case (AKKA / LAA), 6 April 2017, e-Competitions Bulletin April 2017, Art. N° 83821.

¹⁸¹ *General Motors Continental NV v Commission* Case 26/75 [1975].

¹⁸² Commission decision COMP/36.915 – *Deutsche Post AG – Interception of cross border mail* [2001].

¹⁸³ *F. Lucazeau v Société des Auteurs, Compositeurs et Editeurs de Musique* Cases 110/88, 241/88 & 242/88 [1989]. See also Case 395/87 *Ministère Public v Tournier* [1989] in which the Court was asked to rule on similar questions concerning the royalties charged by SACEM. See also Case 402/85 *G. Basset v Société des Auteurs, Compositeurs et Editeurs de Musique* [1987], an earlier preliminary ruling case in which the Court stated that Article 102 can apply to a royalty which is unfair, but did not rule on possible assessment criteria.

¹⁸⁴ *Corinne Bodson v SA Pompes funèbres des régions libérées* Case 30/87 [1988].

¹⁸⁵ Commission decision COMP/36.568 – *Scandinlines Sverige AB v Port of Helsingborg* [2004].

¹⁸⁶ *United Brands Co. v Commission* Case C-27/76 [1978].

¹⁸⁷ OECD, (2011). Excessive Prices. Document submitted to Working Party No. 2 of the Competition Committee. DAF/COMP/WP2/WD(2011)54.

that exists between maintaining low prices and the undertaking of investments in technology and innovation.

282. Furthermore, the OFC opines that while the *United Brands Test* is an indication of excessive pricing, one would also need to consider other important benchmarks as explained in previous paragraphs of this report. The next sub-sections explore these benchmarks in detail.

I. Comparing the Prices of MDP’s Fresh Milk products with the Prices of Other Fresh Milk Products Sold Locally

283. Reference is being made to the new recommended consumer prices of Benna fresh milk products outlined in table 27. The analysis here is focusing on recommended consumer prices rather than MDP’s selling price to the distributor.

Table 27: Revised Recommended Consumer Prices of Benna’s Fresh Milk Products

Product	Recommended Consumer Price as from 29/07/19
Whole Milk 1L	€0.96
Milk 2.5% fat 1L	€0.94
Skimmed Milk 1L	€0.92
Lactose Free Milk 1L	€1.15
Whole Milk ½L	€0.56
Milk 2.5% fat ½L	€0.54
Skimmed Milk ½L	€0.52
Lactose Free Milk ½L	€0.65

Source: MDP’s Official Statement published on 23 July 2019 titled ‘Adjustments to the Prices of Benna Fresh Milk’.

284. Reference is also being made to the request for information sent by the OFC to a selected sample of large grocery retail stores in Malta on 11 September, 2020 whereby Lasco Supermarket, Smart Supermarket, Iceland Supermarket, Trolees Supermarket, Park Towers and Lidl Malta Ltd noted that they supply and/or have supplied fresh milk products other than those manufactured by MDP in the last four years.

285. Collectively, they indicated the following list of products ranked in ascending order based on price:

Table 28: Consumer Prices of Fresh Milk Products other than those supplied by Benna

Product	€/Ltr
Fude & Serrahn Fresh Milk 1.5% Non-OGM	0.72
Fude & Serrahn Fresh Milk 3.5% Non-OGM	0.74
Gropper Whole Milk 1Ltr	0.75
Padania Alimenti Microfiltered Fresh Milk 1.5%	0.85
Padania Alimenti Lactose-free Fresh Milk 1.5% Non-OGM	0.98
Padania Alimenti Semi-Skimmed Microfiltered Milk	0.99
Sole Semi Skimmed Milk 1 Ltr	1.06
Latteria Soresina Semi-Skimmed Fresh Milk 1Ltr	1.08
Cravendale Purifltre Fresh Whole Milk 2 Ltr	1.12
Cravendale Semi-Skimmed Milk 2 Ltr	1.12
Latteria Soresina Whole Fresh Milk 1Ltr	1.15
Padania Alimenti Epiu Whole Organic Milk Microfiltered	1.21
Gropper Organic Fresh Milk 3,8%	1.24
Parmalat Semi-Skimmed Milk Puro Blu 1 Ltr	1.24
Parmalat Puro Blu Latte Intero 1 Ltr	1.35
Parmalat Zymil Latte 1% Alta Digeribilita 1 Ltr	1.35
Granarolo Latte Intero 1Ltr	1.49
Carrefour Bio Partially Skimmed Milk 1 Ltr	1.52
Parmalat Zymil Lactose Free Milk 1 Ltr	1.60
Mountain Farm Fresh Milk 0.7% 1 Ltr	1.83
Pascual Milk Lactose Free 1 Ltr	1.92
Flora Pro Active Milk 1Ltr	1.99
President Half Skimmed Milk 1 Ltr	2.17
Flora Pro Active Milk Low Cholesterol	2.89

Source: Data collected from the RFI sent by the OFC on 11 September, 2020; Author's Calculations.

286. When comparing data from tables 27 and 28, one can realize that the fresh milk products supplied by Benna compare relatively well in terms of price with the other fresh milk products not supplied by Benna. With the exception of Fude and Serrahn, Gropper and one product from the Padania range, Benna fresh milk products are the cheapest when compared to the range of fresh milk products available on the local market. It is noteworthy that the fresh milk products listed in table 28 are fresh milk products which were supplied by retailers over the last four years. As a result, it could well be the case that some of these products are no longer made available by the retailers or the price indicated could have changed.

287. Furthermore, in their submissions dated 2 September, 2019, MDP noted the following products as being close substitutes to Benna fresh milk (table 29).

288. As can be noted from table 29, all the products highlighted by MDP as being close substitutes to the local fresh milk product are all long-life and as a result, according to the findings

of the OFC should not be constituted as forming part of the same relevant market as that of fresh milk. Notwithstanding this, the price of the local fresh milk product still compares relatively well when compared to the highlighted products.

Table 29: Substitutes to Benna Fresh Milk according to MDP

Skimmed Milk Products	€
Milbona UHT	0.65
Arla UHT	0.66
Benna Fresh	0.92
Milcow UHT	1.01
Frisian Flag UHT	1.19
Parmalat UHT	1.25
Dairy Pride UHT	1.29

Semi-Skimmed Milk Products	€
Arla UHT	€0.66
Milbona UHT	€0.69
Benna Fresh	€0.94
Avonmore UHT	€0.99
MILK LDM UHT	€0.99
Tesco UHT	€1.02
Frisian Flag UHT	€1.24
Latteria UHT	€1.25
Dairy Pride UHT	€1.34

Whole Milk Products	€
Milbona ESL	€0.70
Milbona UHT	€0.75
Benna Fresh	€0.96
MILK LDM	€0.99
Tesco UHT	€1.02
Oldenburger UHT	€1.09
Avonmore UHT	€1.12
Frisian Flag UHT	€1.45

Lactose Free Milk Products	€
Benna Fresh	€1.15
Latteria	€1.19
MILK LDM ESL	€1.29
Parmalat SK UHT	€1.54
Granarolo SS UHT	€1.69
Parmalat WH UHT	€1.99
Arla UHT	€2.26

Source: MDP submissions dated 2 September 2019.

II. Comparing the Prices of MDP's Fresh Milk products with the Prices of Fresh Milk Products in the EU

289. According to submissions made by MDP dated 2 September, 2019, it was highlighted that the price of Benna fresh milk is competitive when compared with the price of branded fresh milk¹⁸⁸ available in other Mediterranean countries. In fact, MDP presented the data in table 30:

Table 30: Consumer Price of Fresh Milk in the Mediterranean

Mediterranean Country	Price per Litre	% Difference when compared to Benna Milk
Malta (Benna)	€0.94	
Italy	€1.09 - €1.25	Between +15.96% and +32.98%
Spain	€0.85	-9.57%
Cyprus	€1.37 - €1.40	+45.74%
Greece	€1.16 / €1.23 / €1.50	Between +23.4% and +59.57%
France	€1.10	+17.02%

Source: MDP submissions dated 2 September 2019.

290. Furthermore, according to submissions made by MDP dated 19 November, 2019, the revised retail prices are still competitive when compared to countries and regions with similar characteristics as Malta. They noted that the range of prices in Sicily, Cyprus, Balearic Islands and Sardegna are the following:

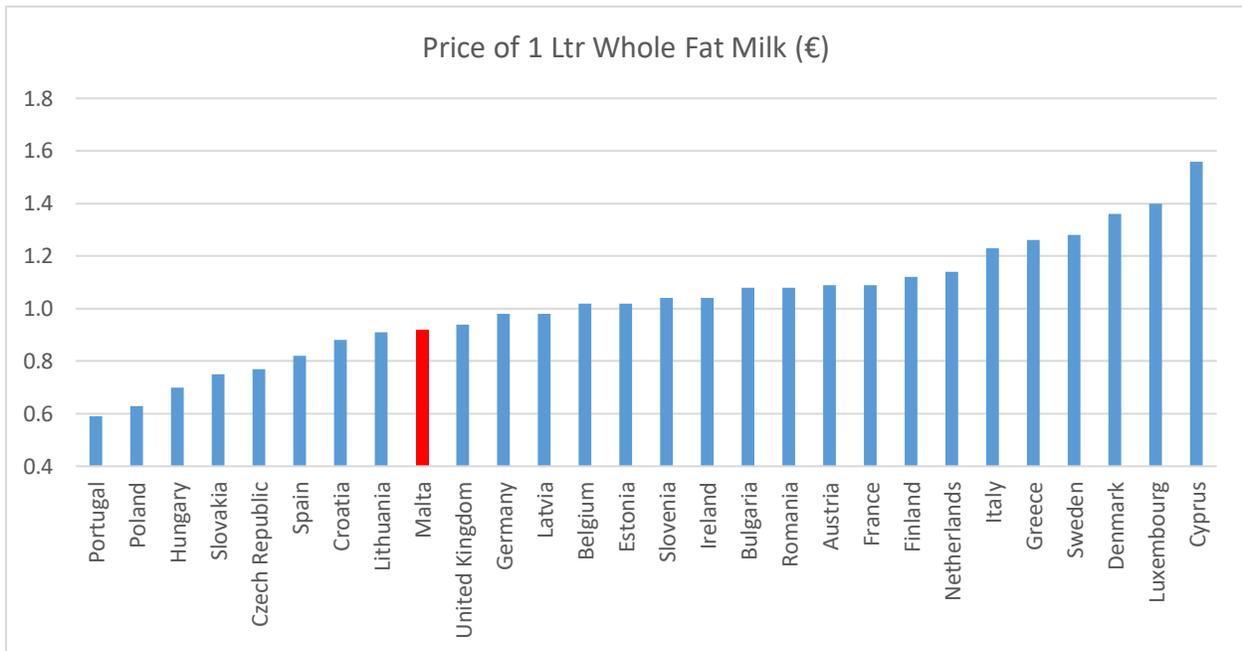
- Sicily: €0.60 to €1.20
- Cyprus: €1.15 to €1.50
- Balearic Islands: €0.70 to €1.10
- Sardegna: €0.80 to €1.00

291. Similarly, the same conclusion could be reached when comparing the average price of 1Ltr Fresh Whole Fat milk in Malta vis-à-vis the price of the same product in the countries of the EU.¹⁸⁹ The data is depicted in Figure 9. Out of the EU28, Malta ranks ninth from bottom, only second to Portugal, Poland, Hungary, Slovakia, Czech Republic, Spain, Croatia and Lithuania.

¹⁸⁸ MDP noted that the prices were obtained from different sources including contacts with dairy sectors in Europe, study by web comparison website 'Compare My Mobile' and published by Malta Today, <https://www.expatisitan.com/cost-of-living/country> and <https://www.numbeo.com/cost-of-living/country> result.jsp?country=Cyprus.

¹⁸⁹ Fresh Whole Fat Milk is the standard milk beverage reported by *Expatisitan*.

Figure 10: Price of 1Ltr Fresh Whole Fat Milk



Source: Expatistan. Data accessed on 21 October, 2020.

III. A Time-Series Analysis of the Prices of MDP’s Fresh Milk products

292. In their submissions, MDP highlighted the following changes in the selling prices of Benna’s fresh milk products to distributors (table 31) and in the recommended consumer prices (table 32).

Table 31: MDP's Selling Price Increases of Benna's Fresh Milk Products to Distributors

Product	Selling Price to Distributor 04-01-11	Selling Price to Distributor 05-01-11	Selling Price to Distributor 04-06-12	Selling Price to Distributor 01-08-12	Selling Price to Distributor 01-06-19	Selling Price to Distributor 01-08-19
Whole Milk 1L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Milk 2.5% fat 1L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Skimmed Milk 1L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Lactose Free Milk 1L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Whole Milk ½L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Milk 2.5% fat ½L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Skimmed Milk ½L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Lactose Free Milk ½L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: Decision of the Office for Fair Competition (Case COMP-CCD/7/11); MDP submissions, dated 12 September 2019.

Table 32: MDP's Recommended Consumer Price of Benna Fresh Milk Products

Product	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Whole Milk 1L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Milk 2.5% fat 1L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Skimmed Milk 1L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Lactose Free Milk 1L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Whole Milk ½L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Milk 2.5% fat ½L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Skimmed Milk ½L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Lactose Free Milk ½L	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: MDP submissions, dated 19 November 2019.

293. As can be noted from tables 31 and 32, the prices of Benna fresh milk products have remain unchanged since 2012.

294. MDP also highlighted that the increase made by MDP in the selling prices of Benna fresh milk are all within the increases in the Food Inflation Index within the Harmonised Index of Consumer Prices as measured by Eurostat, which registered an increase of 14% in the period 2012-2018.

IV. Economic Value of Fresh Milk Products and their Importance to Consumers

295. Fresh milk products do not have substitutes and as a result, aggregate demand is commonly considered to be price inelastic (Bouamra-Mechemache et al. 2008). Furthermore, fresh milk is a staple food product for local consumers and a basic element for one's nutrition as backed by the high percentages inferred from the demand-side survey. The OFC opines that Benna fresh milk can be considered a habitual product for a large customer base, providing a distinctive product for the local market.

296. The OFC opines that the dairy milk sector in Malta is very important as it accounts for around 500 direct jobs along the supply chain of fresh milk, with important synergies with the other agricultural sectors.

297. As a result, the OFC assigns high economic value to the local fresh milk product.

V. Economic or Other Risks Associated with Bringing the Product to the Market and the Investment of Capital and other Resources necessary to bring the products to the Local Market

298. There are a number of risks associated with bringing fresh milk to the market. From the first stage of the supply chain, local herdsmen need to make sure that their farms are managed at the highest standards, ensuring high levels of cleanliness in all the equipment used for raw milk production. Furthermore, herdsmen need to keep their cows healthy by ensuring that a proper diet is being consumed on a daily basis. Failure to do so will risk attaining the standard required levels of fat, protein, SCC and TBC which are necessary in order for raw milk to be eligible for processing.

299. From its end, MDP needs to ensure that the manufacturing process from beginning to end satisfies the required environmental and HACCP quality standards. This can only be ensured by continuous investments to improve quality and production efficiencies through the application of latest technologies. Furthermore, MDP also need to make sure that their products satisfy food safety standards as mandated by the Food Safety Act (2002), Chapter 449 of the Laws of Malta. Moreover, the production process employed by MDP needs to abide with the standard requirements which govern manufacturing processes in Malta.

300. Given that fresh milk needs to be kept refrigerated at all times, the distributors of fresh milk need to make sure that their transport vehicles are properly refrigerated. The same applies for the retailers. A hiccup at a particular stage along the supply chain can cause detrimental effects on consumers' health and welfare.

301. Furthermore, there are a number of capital investments which are required in order to supply fresh milk products on the local market. Apart from the investments which are continuously undertaken by local herdsmen to continue meeting EU hygiene and quality standards for dairy farms, significant investments have been undertaken by MDP in the past years. Apart from the €17.3 million investment by 2013 for the upgrading of facilities at MDP's production plant, MDP will be making an investment in new dairy and ancillary operation totaling [redacted] million. This investment is expected to improve quality and production efficiencies through the application of latest technologies. It will facilitate the introduction of new dairy products on the market by introducing feasible short production runs and will enable the company to continue meeting, efficiently and economically, the required environmental and HACCP quality standards¹⁹⁰. Last but not least, there are investments at the distribution stage, mainly involving transport vehicles.

VI. Assessment of Economic Profitability

302. Another important benchmark used in the determination of excessive pricing involves assessing whether the firm is '*reaping trading benefits that it would not reap under conditions of normal and sufficiently effective competition.*'¹⁹¹ In other words, the assessment involves looking as to whether the firm is earning excessive profits.

303. In their submissions, MDP attributed the loss suffered in 2018 primarily to the continued increases in the cost of raw materials. MDP noted that if the situation seen in 2018 had to persist, MDP's presence in the market will be compromised. Furthermore, it was noted that recurring performances as that seen in 2018 would prevent MDP from undertaking the envisaged investments in its pipeline. Such investments are necessary for MDP to continue sustaining its operations in future years.

304. In their submissions, MDP noted that for the above reasons, it was decided to increase the retail prices of its products. In fact, the above reasons are key in justifying the increase in retail prices of fresh milk effected in 2019.¹⁹²

305. Despite the price increases, MDP expects to continue operating at low mark-ups. In fact, in order to test this, the OFC estimated the total profit expected from the increase in the retail prices of fresh milk by assuming the same level of sales registered in 2018 for 2019. As highlighted in the tables below, by calculating the difference in net profit at unit level, the OFC concludes that had MDP retained the retail prices of fresh milk as they were before the price increase, MDP would have registered a loss of [redacted]. The retail price increases of fresh milk are expected to yield MDP an operating profit of [redacted], an increase of [redacted] when compared to the pre-price increase scenario.

¹⁹⁰ Source: MDP submissions, dated 19 November 2019.

¹⁹¹ Ibid, paragraph 443.

¹⁹² Source: MDP submissions, dated 2 September 2019.

Table 33: MDP's Change in Annual Earnings expected from the increase in the retail prices of fresh milk

	Whole 1L	2.5% Fat 1L	Skimmed 1L	Lactose Free 1L	Whole 0.5L	2.5% Fat 0.5L	Skimmed 0.5L	Lactose Free 0.5L
Net Profit in €/unit pre-price increase (01-01-2019)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Net Profit in €/unit post-price increase (29-07-2019)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Difference in Net Profit per Unit	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Annual Sales in Units (based on 2018 figures)	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]
Total Profit Post-Price increase	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]	[✂]

Source: MDP submissions, dated 2 September 2019; Author's calculations.

306. In order to put these figures in perspective, the table below presents the net profit margin of MDP at product category.

Table 34: MDP's Net Profit Margin in Fresh Milk Products

	Whole 1L	2.5% Fat 1L	Skimmed 1L	Lactose Free 1L	Whole 0.5L	2.5% Fat 0.5L	Skimmed 0.5L	Lactose Free 0.5L
Selling Price to Distributors in €/unit	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Net Profit in €/unit post price increase (29-07-2019)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Net Profit Margin (%)	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

Source: MDP submissions, dated 2 September 2019; Author's calculations.

307. The OFC considers that the fresh milk products could be grouped in three different categories when analysing net profit margins. The OFC views the net profit margin recorded for the Whole 1L, 2.5% fat 1L and Skimmed 1L product categories to be very low, the net profit margins recorded for Skimmed 0.5L, Lactose Free 1L and 2.5% Fat 0.5L to be low and the net profit margins recorded for Lactose Free 0.5L and Whole 0.5L to be moderate.

308. A closer look at the sales reported by MDP in 2018 reveals that the very low profit margin product category accounted for [REDACTED] of the total sales reported by MDP. On the other hand, the moderate profit margin product category only accounted for [REDACTED] of the total sales reported by MDP in 2018. This analysis is depicted in Figure 1 below.

309. As a result, the OFC opines that even with the recent retail price increases of fresh milk, MDP will still retain low profit margins. According to the OFC's calculations, the expected annual profit from the range of fresh milk products is [REDACTED]. This yields an overall expected net profit margin of [REDACTED] which is considered to be very low by business standards.

Figure 11: Sales Fresh Milk Categories - in Units

[REDACTED]

310. It is also worth noting that the above computations by MDP and by the OFC are based on the assumption that MDP retains the 2018 sales figures for 2019. Assuming a naïve forecast is perhaps the best approach one could take under such analysis. However, one is also assuming that the quantity demand for fresh milk is unresponsive to the recent price increases. Furthermore, one is also excluding any changes in quantity demanded attributed to foreseen population changes.

VII. Expected, Probable and/or Possible Changes in the Market for Fresh Milk Products

311. Over recent years, the sector has managed to renew itself and adapt to a number of challenges, amongst which is the adaptation of complex regulations and standards, liberalisation of imports, the removal of protective levies and the dismantling of the quota system in milk production. Partly, these challenges were overcome by significant investments to restructure and upgrade the local milk sector with the aim of increasing efficiency and quality along the supply chain.
312. Going forward, challenges do remain. Competition is expected to intensify over the years to come, attributed to: (i) dairies across the EU are seeking to consolidate and merge, seeking increased market shares as they exploit favourable economies of scale and lower costs of production, (ii) local sector is unable to produce long-life dairy products or milk powder due to the fact that Malta's volume does not justify the investment required to do so, giving opportunities for foreign products to intensify competition in this sub-market, and (iii) local sector is unable to have a safety net provided by EU intervention measures to sustain market instability when supply exceeds demand. Furthermore, the removal of the quota system is expected to continue strengthening the market position of huge retail businesses across the EU, further limiting the countervailing power of primary producers.¹⁹³
313. It is highly likely that the range of concentrated and long-life milk products available in Malta's grocery retail market will continue to increase. While the demand-side survey concluded that these range of products do not form part of the same relevant market as that of fresh milk, however, increased countervailing buyer power from large retailers setting-up shop in Malta and/or increased buyer power from existing retailers is likely to exert new pressures on the local fresh milk product as economies of scale, lower costs and bulk discounts increase the scope for price skimming strategies to gain higher shares in the local market.
314. The local market could well experience an increased number of imported fresh milk products, therefore directly competing with the local product. Depending on the country of origin, these products may have a lower price due to economies of scale. On the other hand, transport costs are likely to outweigh some of the advantages in this regard.
315. While in the years to come, intensified competition is inevitable, natural and structural disadvantages associated with a small island state will persist. These will continue to affect the local costs of production, thereby increasing the opportunity costs for local herdsmen and all those along the supply chain. Furthermore, drought and desertification in Southern Europe are expected to continue affecting locally-grown silage used to feed dairy cows and on-farm consumption of water, thereby increasing costs. Increased volatility of grain prices and increased costs associated with avoiding risk of environmental degradation are also likely to increase the costs of production in the years to come.
316. Continued improvement in farm management, efficiency and quality will be necessary. On its part, MDP needs to continue investing in new market initiatives while KPH needs to continue its efforts to provide strategic direction and support to dairy farmers especially in maintaining and

¹⁹³ P. Von Brockdorff and G. Buttigieg (2015), *Sectoral Impact: An Insight into How the Maltese Dairy Sector Adapted to EU Membership*, Reflection on a Decade of EU Membership, Occasional Paper 06/2015.

improving the performance level reached since EU membership. Such strategies will contribute towards ensuring that competition is not narrowly-defined on the price aspect alone.

D. Conclusion on abuse of dominance

317. The OFC undertook an exhaustive number of assessments in order to assess whether the recent price increases are excessive or not.

318. Following the methodology as set in *United Brands*¹⁹⁴, the OFC concluded that the difference between the costs actually incurred and the price charged is not excessive. This conclusion was reached after determining that the excesses found are not material and/or sufficiently large to be deemed excessive.

319. Furthermore, based on a comparison between the price of Benna fresh milk products with the prices of other milk products found in the local market, the OFC concluded that the price of Benna fresh milk products compare relatively well. The same conclusion is also reached when comparing the price of the local fresh milk product with the price of fresh milk products sold in other Mediterranean and European countries. This is despite the fact that Malta as a small island state is characterised by natural and structural disadvantages which makes it even more challenging for local producers to maintain competitive prices.

320. The OFC has also acknowledged the fact that between 2012 and 2019, the prices of Benna fresh milk products have remained the same despite tantamount upward pressures in costs and that these increases are all within the increases in the Food Inflation Index within the Harmonised Index of Consumer Prices as measured by Eurostat, which registered an increase of 14% over the 2012-2018 period.

321. The OFC also assigns high importance to the economic value of the local fresh milk product and opines that the risks involved in bringing the local fresh milk product to the local market are substantial. The OFC positively recognised that throughout the years, MDP undertook significant investments in order to improve its operations and product quality, reduce costs, improve efficiency and widen its product portfolio. Going forward, MDP is planning another round of investments which would put MDP in a position to continue meeting consumers' needs and expectations and make the company more competitive.

322. The OFC notes that even with the recent increase in selling prices, the profit margin of the company's fresh milk product is moderate and that its two main products which account for a sizeable portion of MDP's turnover, namely Fresh Milk 2.5% fat 1Ltr and Fresh Skimmed Milk 1Ltr only have a margin of [X] and [X], respectively.

323. Based on a naïve forecast, the OFC concludes that even with the recent increase in selling prices, MDP's annual profit from the fresh milk category will be in the region of [X]. This yields an overall expected net profit margin of [X] which is considered to be very low by business standards.

¹⁹⁴ *United Brands v Commission*. Case 27/76. Court of Justice, [1978] 1 CMLR 429.

Section 4: Effect on Trade between EU Member States

324. Where the OFC applies national law to an abuse of a dominant position which has an effect on trade between EU Member States, the OFC must also apply Article 102 of the TFEU.¹⁹⁵

325. Article 102 of the TFEU (ex Article 82 TEC) prohibits ‘*any abuse by one or more undertakings of a dominant position **within the internal market or in a substantial part of it...** in so far as it **may affect trade between Member States.***’ [Emphasis Added]

326. For the purpose of assessing whether trade between EU Member States may be affected, the OFC follows the approach set out in the Commission’s Guidelines on the effect on trade concept contained in Articles 81 and 82 of the Treaty¹⁹⁶ and the case law of the European Courts.

327. As highlighted in *Compagnie Maritime Belge v Commission*:¹⁹⁷

*‘It should first be recalled that it has been consistently held that, in order that an agreement between undertakings, or moreover an abuse of a dominant position, **may affect trade between Member States, it must be possible to foresee with a sufficient degree of probability and on the basis of objective factors of law or fact that it may have an influence, direct or indirect, actual or potential, on the pattern of trade between Member States, such as might prejudice the realization of the aim of a single market in all the Member States.***¹⁹⁸ Accordingly, it is not specifically necessary that the conduct in question should in fact have substantially affected trade between Member States. It is sufficient to establish that the conduct is capable of having such an effect.’¹⁹⁹ [Emphasis Added]

328. As highlighted in the *Effect on Trade Guidelines*, an effect of trade between EU Member States is more likely to exist when by their nature products are easily traded across borders.²⁰⁰ Trade between EU Member States may also be effected in cases where the relevant market is national or sub-national.²⁰¹

329. On the basis of the evidence collected, the OFC is of the opinion that given that the fresh milk produced by MDP is produced locally and distributed and sold in every location of Malta, then the criteria which calls for ‘...*within the internal market or in a substantial part of it...*’ is satisfied. Nonetheless, the OFC is of the opinion that given the fact that raw milk is wholly produced, distributed and sold locally, then the activities are not cross-border in nature. However, the OFC acknowledges that the concept is not limited to the traditional trading of goods across borders but encompasses wider concepts covering all cross-border economic activity including establishment.²⁰²

¹⁹⁵ Article 3 of Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty.

¹⁹⁶ Guidelines on the effect on trade concept contained in Articles 81 and 82 of the Treaty, OJ C 101, 27.4.2004, p.81 to 96.

¹⁹⁷ *Compagnie Maritime Belge v Commission*. Case T-24/93. Court of Justice, [1996] ECR II-1201, paragraph 201.

¹⁹⁸ *Gøttrup-Klim and Others Grovwareforeninger v Dansk Landbrugs Grovvareselskab*. Case C-250/92 DLG [1994] ECR I-5641, paragraph 54

¹⁹⁹ See, as regards [Article 102 TFEU], Joined Cases C-241/91 P and C-242/91 P RTE and ITP v Commission [1995] ECR I-743, paragraph 69.

²⁰⁰ Effect on Trade Guidelines, paragraph 30.

²⁰¹ *Ibid*, paragraph 22.

²⁰² Effect on Trade Guidelines, paragraph 19. See also, for example, the judgment in *Züchner v Bayerische Vereinsbank* C-172/80, EU:C:1981:178, paragraph 18.

330. As *Hugin v. Commission*²⁰³ demonstrates, when trade is inherently localised in one member state, the conduct lacks appreciable effect on inter-state trade.

331. Nevertheless, with regards to excessive pricing in the context of Article 9 of the Competition Act and Article 102 of the TFEU, the OFC considers that since the legal requirements of Article 9 were not satisfied, neither Article 102 comes into play.

Section 5: Decision of the OFC

332. For the above-mentioned reasons:

The OFC hereby declares that it finds no evidence from MDP's part of infringing Article 9 of the Competition Act and finds no grounds for action regarding Article 102 of the TFEU regarding the prices of Benna fresh milk products.

333. The OFC also declares that:

- given that the consumer prices of Benna's fresh milk products compare relatively well both with other products in the local market and also with like products in neighbouring markets, and
- that the difference between the selling price of fresh milk to the distributors and the final consumer price is a weighted average of [] of the final consumer price, which difference is further split between the distributors and the retailers,

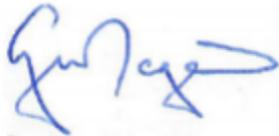
the OFC does not feel the need to investigate distributors and retailers.

²⁰³ *Hugin Kassaregister AB and Hugin Cash Registers Ltd v Commission of the European Communities*. Case 22/78.

Signed by the following:



Mr. Gilmour Camilleri,
Director Communications, Energy, Transport and Financial Services,
for and on behalf of the Office for Competition; and



Mr. Godwin Mangion,
Director General,
for and on behalf of the Office for Competition.

The report has been compiled by the leading investigator, Mr. Gilmour Camilleri.

For any questions on the contents of this case, please do not hesitate to contact the undersigned.

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Annex A: Milk Consumption Survey

Start of Block: CONSENT

Q1.1 Interviewer Identifier Number

Q1.2

Good day, Sir/Madam. Do you prefer to speak in English or Maltese?

Note for Interviewers: DO NOT PROVIDE ANSWERS UNLESS OTHERWISE STATED; KEEP NOTE OF ANY ADDITIONAL INFORMATION WHICH RESPONDENT OFFERS. ADD AS NOTES AT THE END OF THE INTERVIEW

Maltese (1)

English (2)

Q1.3

My name is _____ and, on behalf of the Office for Competition, I would like to invite you to participate in a telephone interview.

The information you provide will be used for research on milk consumption and if you would like to discuss this research you may contact the Office for Competition at MCCA at any point and ask for Mr. Godwin Mangion, Director General (Office for Competition): godwin.mangion@mccaa.org.mt

Allow me also to inform you that your telephone number has been selected randomly and your participation is voluntary. You will not be asked your name at any time, and the answers you give cannot identify you.

You may refuse to answer any question and quit the survey at any time without any problem.

The interview takes about 10 minutes to complete. Would you like to continue?

NOTE FOR INTERVIEWERS: If respondents say "NO", ASK IF YOU MAY call them later, set an appointment, quit the INTERVIEW AND THANK THEM. If they do not wish to set an appointment, QUIT AND THANK THEM. If you tick "no" the survey ends.

Yes (1)

No (2)

Skip To: End of Survey If Q1.3 = 2

End of Block: CONSENT

Start of Block: DEMOGRAPHICS

Q2.1 In your household what is the total number

	0 (1)	1 (2)	2 (3)	3 (4)	4 (5)	5 (6)	6 (7)	7 (8)	8 or more (9)
Of children aged under 16 (1)	<input type="radio"/>								
Of adults (2)	<input type="radio"/>								

Q2.2 What is your nationality?

Maltese (1)

Maltese and Other (2) _____

Other (3) _____

Q2.3 What is your current civil status? (READ ANSWERS)

- Married/Civil Union (1)
- Widowed (2)
- Divorced/Separated/Annulled (3)
- Single (4)
- Cohabiting (5)
- Prefer not to answer (6)

Q2.4 Which is the highest level of education you have successfully completed? (READ ANSWERS)

- No Schooling (1)
- Pre-Primary (2)
- Primary (3)
- Special School for Disabilities (4)
- Secondary (5)
- Post Secondary (6)
- Tertiary or Higher (7)

Q2.5 Which of the following best describes your current labour status? (READ ANSWERS)

- Student/Trainee (1)
- Seeking a job (2)
- Employed (3)

- Unemployed (4)
- Cannot work (5)
- Housewife/Homemaker (6)
- Retired (7)
- Inactive (8)

End of Block: DEMOGRAPHICS

Start of Block: DEFINING THE RELEVANT MARKET

Q3.1 In the past month, have you or anyone in your household consumed milk? (NOTE THAT HERE WE ARE REFERRING TO UNFLAVOURED LIQUID MILK) (READ ANSWERS)

- Yes (1)
- No (2)

NOTE FOR INTERVIEWERS: If respondents say "NO", skip directly to question 6.1.

Q3.2 On average, how often did you or anyone in your household consumed milk?

- Never (1)
- Less than once a week (2)
- 1 to 2 times a week (3)
- 2 to 3 times a week (4)

- 4 to 5 times a week (5)
- Daily (6)
- More than once a day (7)

Q3.3 For what purposes, did you or anyone in your household consumed milk?

- As a beverage on its own (1)
- With cereal (2)
- With hot beverages (3)
- Cooking purposes (4)
- Other _____ (5)

Q3.3 What type of milk do you or anyone in your household usually consume? (Note that the respondent can indicate more than one option)

- Fresh Milk (1)
- Concentrated Milk (e.g. Powdered Milk) (2)
- Long-Life Milk (3)

NOTE FOR INTERVIEWERS: If respondents do not mention "Fresh Milk", skip directly to question 3.7

Q3.4 In the case of fresh milk, do you buy the local Benna product?

- Yes (1)
- No (2)

Q3.5 What type of fresh milk do you or anyone in your household usually consume? (Note that the respondent can indicate more than one option)

- Fresh Whole Milk (1)
- Fresh Milk 2.5% fat (2)
- Fresh Skimmed Milk (3)
- Fresh Lactose Free Milk 2.5% fat (4)
- Flavoured Milk (e.g. Strawberry, Chocolate, Coconut Milkshake, etc.) (5)
- Other _____ (6)

Q3.6 What size of fresh milk do you usually buy?

- 500ml (1)
- 1 litre (2)
- Other _____ (3)

Q3.7 Are you aware of how much it costs to buy a 500ml fresh local produce milk carton?

- Yes (1)
- No (2)

NOTE FOR INTERVIEWERS: If the respondent answers "Yes", skip question 3.9 whereas if the respondent answers "No", skip question 3.8.

Q3.8 If yes, how much?

- Price _____

Q3.9 If not, can you guess?

Price _____

Q3.10 Are you aware of how much it costs to buy a 1 litre fresh local produce milk carton?

Yes (1)

No (2)

NOTE FOR INTERVIEWERS: If the respondent answers "Yes", skip question 3.12 whereas if the respondent answers "No", skip question 3.11.

Q3.11 If yes, how much?

Price _____

Q3.12 If not, can you guess?

Price _____

Q3.13 On a scale of 1 to 5 (1 = Strongly Disagree and 5 = Strongly Agree), state to what extent do you agree with this statement: I am fully aware of the nutritional difference/health benefits that exist between Long-Life Milk or Condensed Milk and Fresh Milk?

Strongly Disagree (1)

Disagree (2)

Neither disagree nor agree (3)

Agree (4)

Strongly Agree (5)

Q3.14 On a scale of 1 to 5 (1 = Strongly Disagree and 5 = Strongly Agree), state to what extent do you agree with this statement: I am fully aware of the price differences that exist between Long-Life Milk or Condensed Milk and Fresh Milk?

- Strongly Disagree (1)
- Disagree (2)
- Neither disagree not agree (3)
- Agree (4)
- Strongly Agree (5)

Q3.15 On a scale of 1 to 5 (1 = Strongly Disagree and 5 = Strongly Agree), state to what extent do you agree with this statement: I am fully aware of the interchangeability factor in intended use that exists between Long-Life Milk or Condensed Milk and Fresh Milk?

- Strongly Disagree (1)
- Disagree (2)
- Neither disagree not agree (3)
- Agree (4)
- Strongly Agree (5)

End of Block: DEFINING THE RELEVANT MARKET

Start of Block: DEMAND SUBSTITUTION

Q4.1 Do you consider Long-Life Milk or Condensed Milk as a potential substitute to Fresh Milk?

- Yes (1)
- No (2)

Q4.2 What is the reason for answering so?

- Taste reasons (1)
- Health reasons (2)
- Nutritional reasons (3)
- Price reasons (4)
- Other _____ (5)

Q4.3 On a scale of 1 to 5 (1 = Least Important and 5 = Most Important), state to what extent do you assign importance to each of these attributes when choosing milk.

	Least Important (1)	Not Important (2)	Neutral (3)	Important (4)	Very Important (5)
Price					
Quality					
Freshness					
Availability					
Duration of Product					
Nutrition					
Health					
Intended Use					

Q4.4 On a scale of 1 to 5 (1 = Strongly Disagree and 5 = Strongly Agree), state to what extent do you agree with the following statements:

	Strongly Disagree (1)	Disagree (2)	Neither disagree nor agree (3)	Agree (4)	Strongly Agree (5)
I prefer not to buy any milk if Fresh Milk is not available					
I only use Long-Life/Condensed Milk when Fresh Milk is not available					
I prefer to consume Long-Life/Condensed Milk because it is more convenient and saves me shopping time (long-lasting)					
In my opinion, Fresh Milk and Long-Life/Condensed Milk have the same taste					
I do not consume Long-Life/Condensed Milk because it is more expensive than Fresh Milk					
I prefer Fresh Milk because I perceive it as healthier than Long-Life/Condensed Milk					
Consumers have a wide variety of Fresh Milk to choose from					
Up to now I have never consumed Long-Life/Condensed Milk					
I am not willing to consume Long-Life/Condensed Milk					

End of Block: DEMAND SUBSTITUTION

Start of Block: DEMAND SUBSTITUTION QUESTIONS - EXCESSIVE PRICING

NOTE FOR INTERVIEWERS: If the respondent answered “Concentrated Milk” or “Long-Life Milk” in question 3.3 and/or “No” in question 3.4, skip directly to Question 5.7.

Q5.1 On 23rd July 2019, Benna announced that the price of fresh milk is set to increase with effect from 29th July 2019. On average, the increases amounted to 11c for the 1L cartons and 7c for the 500ml cartons. Following these price increases, do you intend to continue consuming locally produced Benna fresh milk?

Yes (1)

No (2)

Q5.2 Imagine that the price of locally produced Benna fresh milk had to increase by 10% or by around 9c for the 1L carton and by around 5c for the 500ml carton. On a scale of 1 to 5 (1 = Highly Unlikely and 5 = Highly Likely), to what extent would you:

	Highly Unlikely (1)	Unlikely (2)	Neutral (3)	Likely (4)	Highly Unlikely (5)
Switch to foreign fresh milk products					
Switch to Condensed/Long-Life Milk					
Reduce the overall consumption of milk					
Be willing to at least, try switching for Condensed/Long-Life Milk					

Q5.3 Imagine that the price of locally produced fresh milk had to increase by 20% or by around 19c for the 1L carton and by around 11c for the 500ml carton. On a scale of 1 to 5 (1 = Highly Unlikely and 5 = Highly Likely), to what extent would you:

	Highly Unlikely (1)	Unlikely (2)	Neutral (3)	Likely (4)	Highly Unlikely (5)
Switch to foreign fresh milk products					
Switch to Condensed/Long-Life Milk					
Reduce the overall consumption of milk					
Be willing to at least, try switching for Condensed/Long-Life Milk					

Q5.4 Imagine that the price of locally produced fresh milk had to increase by 10% and at the same time, the price of Condensed/Long-Life Milk decreases by 5%. On a scale of 1 to 5 (1 = Highly Unlikely and 5 = Highly Likely), to what extent would you:

	Highly Unlikely (1)	Unlikely (2)	Neutral (3)	Likely (4)	Highly Unlikely (5)
Switch to foreign fresh milk products					
Switch to Condensed/Long-Life Milk					
Reduce the overall consumption of milk					
Be willing to at least, try switching for Condensed/Long-Life Milk					

Q5.5 What would be the maximum price which you are willing to pay to keep on consuming locally produced fresh milk (per litre)?

€ _____

Q5.6 What would be the maximum price which you are willing to pay to keep on consuming locally produced fresh milk (per litre) before considering switching to Condensed/Long-Life Milk?

€ _____

Q5.7 At what price would you consider switching to locally produced fresh milk (per litre)?

€ _____

End of Block: DEMAND SUBSTITUTION QUESTIONS - EXCESSIVE PRICING

Start of Block: Conclusion

Q6.1 How old are you?

Q6.2 What is your gender?

- Male (1)
- Female (2)
- Other (3)
- Prefer not to answer (4)

Q6.3 In which locality do you live?

▼ Attard (1) ... Żurrieq (68)

Q6.4 Region

Note to Interviewer: TO BE FILLED IN BY INTERVIEWER - NOT TO BE READ OUT LOUD

- Northern (1)
- Western (2)
- Northern Harbour (3)
- Southern Harbour (4)
- South Eastern (5)
- Gozo (6)

On behalf of the Office for Competition, I would like to thank you for your time in responding to our questionnaire. Kindly note that your responses will remain confidential and will only be used for internal purposes only. If you have further comment which you would like to make, please do not hesitate to put them forward.

If not, thank you for your patience and information. Have a good day/evening.

End of Block: CONCLUSION
