



THE ONLINE MAGAZINE FOR GLOBAL COMPETITION POLICY

The InBev and Anheuser-Busch Merger in China: A View from Economists

Xinzhu Zhang, Vanessa Yanhua Zhang, and Howard Chang

Chinese Academy of Social Sciences & LECG Consulting,
LLC

The InBev and Anheuser-Busch Merger in China: A View from Economists

Xinzhu Zhang, Vanessa Yanhua Zhang, and Howard Chang *

On November 18, 2008, China's Ministry of Commerce ("MOFCOM"), the Chinese merger control authority, approved InBev's takeover of Anheuser-Busch, with certain restrictions.¹ The InBev Decision is the only published decision that MOFCOM has made to date following the implementation of China's Anti-Monopoly Law ("AML") in August 2008.² As such, it has attracted the interest of international antitrust scholars and practitioners. In this paper, we provide some background on the merger approval process in China and the InBev acquisition, and then discuss the implications of MOFCOM's decision and its other statements on merger policy for the future of merger control in China.

* Xinzhu Zhang is the Director of the Research Central for Regulation and Competition (RCRC), the Chinese Academy of Social Sciences. He is also a Director of the Global Competition Policy Practice at LECG Consulting, LLC, an economic and management consulting company, in Beijing. Vanessa Yanhua Zhang is a Senior Economist of the Global Competition Policy Practice at LECG Consulting, LLC, in Beijing and Chicago. Howard Chang is a Director of the Global Competition Policy Practice at LECG Consulting, LLC, in Chicago. Xinzhu Zhang can be contacted by email at xzzhang@public.bta.net.cn. Vanessa Yanhua Zhang can be contacted by email at vzhang@lecg.com. Howard Chang can be contacted by email at howard_chang@lecg.com.

¹ Announcement No. 95, 2008 of the Ministry of Commerce of the People's Republic of China, November 18, 2008, available at <http://www.mofcom.gov.cn/aarticle/b/c/200811/20081105899353.html>.

² The other seven decisions are believed to have been approved without conditions. See Press Conference of Mr. Ming Shang on the Antimonopoly Investigation in Operators' Concentration, November 21, 2008, available at <http://www.mofcom.gov.cn/aarticle/zhengcejid/bj/200811/20081105906893.html>.

I. LEGISLATIVE BACKGROUND

China's Anti-Monopoly Law was passed by the twenty-ninth session of the tenth National People's Congress on August 30, 2007 and became effective on August 1, 2008.³ The AML is one of the most important laws passed by the Chinese government since China's entry into the WTO and is poised to act as an economic constitution in the Chinese economy. On August 3, 2008 the State Council issued the *Regulation on Notification Thresholds for Concentration of Undertakings* ("Thresholds Regulation"), which sets out the thresholds for pre-merger notification in China.⁴ The AML and the Thresholds Regulation are the legislative bases for the new pre-merger filing system. In addition, MOFCOM has issued the *Guidelines for the Antitrust Filing for Merger and Acquisition of Domestic Enterprises by Foreign Investors* ("Filing Guidelines"), which provide additional guidance on the types of information to be submitted (e.g., market definition, competitive conditions, and entry conditions) by the merging parties. The most recent set of Filing Guidelines were issued in March 2007 and additional related guidelines are being drafted following the passage of the AML.

II. BEER INDUSTRY IN CHINA

The beer industry in China has experienced significant growth and consolidation in recent years. Growth has been driven mainly by increasing income, which has on

³ See Xinzhu Zhang and Vanessa Yanhua Zhang, *The Anti-Monopoly Law in China: Where Do We Stand?*, 3(2) COMPETITION POL'Y INT'L (Autumn 2007) available at <http://ssrn.com/abstract=1075428>.

⁴ PEOPLE'S REPUBLIC OF CHINA, THE REGULATION ON NOTIFICATION THRESHOLDS FOR CONCENTRATION OF UNDERTAKINGS (Aug. 3, 2008) (in Chinese), available at http://www.gov.cn/zwjk/2008-08/04/content_1063769.htm.

average risen 10 percent annually in the last five years.⁵ Lifestyle changes have also contributed to the growth. In 2007, the beer production of the country was 39.3 million tons, an 11.8 percent increase over the previous year. From 1991 to 2007, China's beer production increased by 391 percent, with an average annual growth rate of 10.7 percent.⁶ Major beer companies brought in \$10.5 billion in sales revenue in 2006, and their gross profit reached \$460 million.⁷

The four largest beer companies in China are China Resources Snow Breweries, Tsingtao Breweries, Beijing Yanjing Brewery and Zhujiang Brewery. One estimate places the share of these four companies at around 41 percent of industry revenue currently.⁸ Concentration among beer producers has been increasing in the last few years due to mergers and acquisitions. The share of the ten largest firms increased from 37 percent of total industry revenue in 2001 to 61 percent in 2005.⁹ This trend is expected to increase.

The main categories of Chinese beer consumption are canned beer, bottled beer, keg and draught beer, and other types of beer.¹⁰ The total revenue of the beer industry in

⁵ Source: China Statistical Yearbook (2007), National Bureau of Statistics of China, <http://www.stats.gov.cn/>.

⁶ Source: China's Beer Industry Development of 2008, Report Linker, March 2008, *available at* <http://www.reportlinker.com/p091028/China-s-Beer-Industry-Development-of-2008.html>.

⁷ Source: China Beer Market Report, 2008, Research and Market - China Consulting, May 2008, *available at* http://www.researchandmarkets.com/research/6f0f87/china_beer_market, [1USD=7.9955 CNY as of the conversion rate on July 1st, 2006.]

⁸ Source: China Industry Report - Beer Manufacturing, IBISWorld 2008.

⁹ *Id.*

¹⁰ We provide this information for background and context. There is no discussion in the published Decision as to whether relevant markets or other competitive concerns with respect to these categories of beer were considered.

2007 was \$12.9 billion.¹¹ Sales of canned beer accounted for 40 percent of total revenue. 36 percent of the total revenue came from bottled beer and 14 percent from keg and draught beer. Sales of other types of beer made up the remaining 10 percent of total revenue.¹² The price of canned beer is lower than that of other beer types. Bottled beer and keg and draught beer are more popular in the high-end market, particularly in restaurants, clubs, and hotels. Bottled beer is gaining popularity among residential consumers.

In terms of potential geographic markets, most sales came from East China, the most developed region in China. In 2007, sales revenue in East China was \$8.3 billion, accounting for 39.6 percent of total sales revenues. Sales revenue in Middle South China contributed 25.5 percent of total revenues. North China, Northeast China, Southwest China, and Northwest China beer sales represented 11.2 percent, 10.1 percent, 8.3 percent, and 5.3 percent of the total revenues respectively.¹³

Beer consumption differs significantly across regions. For example, the top three beer manufacturers in Shanghai—Suntory, Reeb, and Bass—accounted for 56 percent of consumption in 2005. Meanwhile, Yanjing, Five Star, and Tsingtao were the top three manufacturers in the Beijing area in the same year, and accounted for 77 percent of consumption.¹⁴ In general, there are no major regulatory or other entry barriers at the national level, but local beer manufacturers may enjoy protection from local governments

¹¹ *Id.*

¹² *Id.*

¹³ *Id.*

¹⁴ J. Slocum et al, “Fermentation in the China Beer Industry”, 35(1) ORGANIZATIONAL DYNAMICS 32-48 (2006).

and entry can be difficult for brands from other regions. Indeed, local protection has contributed to the differences in beer consumption across regions. In order to compete in China, multinational beer companies have most often set up joint ventures with Chinese firms.

III. IMPLICATIONS OF INBEV DECISION

In the InBev Decision, MOFCOM found that the transaction will not eliminate or restrict competition in China's beer market.¹⁵ However, it imposed three main prospective restrictions on InBev post-merger, which will hold significant stakes in two of the four largest beer producers in China. Pre-merger, Anheuser-Busch had a 27 percent stake in Tsingtao Brewery (the second largest producer) and InBev had a 29 percent stake in Zhujiang Brewery (the fourth largest). The first restriction imposed by MOFCOM is that, post-merger, InBev should not increase its stakes from pre-merger levels. Second, InBev may not acquire any stakes in China Resources Snow Breweries or Beijing Yanjing Brewery, the largest and third largest beer producers in China. And third, InBev will be obliged to notify MOFCOM of any changes in its controlling shareholders.

While the InBev Decision does not provide a lot of detail on MOFCOM's underlying analysis, based on our reading of the Decision, the AML and Filing Guidelines, as well as the statements of Mr. Shang, MOFCOM's Director,¹⁶ we have

¹⁵ The Decision used the terms "market" and "market share" to describe the shares of beer producers in China but did not present any additional discussion of market definition.

¹⁶ *Supra* note 2.

some tentative thoughts on its implications for the merger control process in China going forward.

First, the timing and circumstances of InBev's clearance in "Phase 1" is interesting. The parties submitted information and responded to requests from MOFCOM prior to formally entering the 30 day Phase 1 period.¹⁷ These discussions included consideration of potential remedies,¹⁸ which indicates that MOFCOM is open to a substantive dialogue early on. Developing an advance understanding of potential concerns that MOFCOM is likely to have and having a plan for restrictions that are acceptable to the merging parties is important.

Second, in the process of reviewing the merger, MOFCOM states that it gathered information through phone calls, in-person meetings, and public hearings. It contacted a wide range of interested parties, including relevant governmental departments, local governments, the brewery industry association, the major domestic beer makers, input suppliers and distributors. Merging parties should consider the likely issues that will be raised by all of the parties that MOFCOM is likely to contact on a given transaction. For example, MOFCOM appeared to be convinced that competition among beer producers in China is generally robust. But it may well have been concerned by the trend of increasing concentration and the high concentration already present in some local regions. These concerns may have motivated the imposed restrictions in MOFCOM's clearance decision.

¹⁷ InBev's initial submission was on Sep 10; further supplements were submitted on Oct 17 and 23; and MOFCOM initiated phase 1 on Oct 27. *Supra* note 1.

¹⁸ *Supra* note 2.

Third, it is important that merging parties provide convincing economic evidence and analysis to MOFCOM, especially with respect to areas that are of potential concern. The Director of MOFCOM has indicated that economists are deeply involved in the review process before any decisions are reached and that the economic analysis department of the Anti-Monopoly Bureau will need more economists and industry experts in the near future.¹⁹ Even though some noneconomic factors such as national security may be considered in a given transaction, economic analysis will play a major role in merger clearance.

Fourth, local competitive conditions and concerns matter. The restrictions imposed by MOFCOM were necessary to address its specific concerns about the overlap between Tsingtao Brewery and Zhujian Brewery resulting from Anheuser-Busch and InBev's ownership stakes. This merger has also been cleared in the United States and the United Kingdom, with each competition authority taking a different approach in considering the local issues in the respective jurisdictions. In the United States, the Department of Justice imposed the divestiture of InBev's sales force, Labatt USA, in order to ensure that "consumers will continue to benefit from the significant competition between the merging companies in upstate New York."²⁰ The Office of Fair Trade in the United Kingdom cleared the merger without imposing any restrictions. The OFT's preliminary concerns focused on the on-trade channel, but it eventually found "there was

¹⁹ Interview with Mr. Ming Shang, Director of the Anti-Monopoly Bureau, MOFCOM, December 5, 2008, available at <http://www.gov.cn/zxft/ft155>.

²⁰ Statement of Deborah A. Garza, Deputy Assistant Attorney General of the Antitrust Division, Department of Justice Press Releases, November 14, 2008, available at http://www.usdoj.gov/atr/public/press_releases/2008/239430.htm.

no realistic prospect that drinkers of Stella, Beck's, or Bud would pay more as a result of this merger."²¹

And fifth, the imposition of the restrictions on InBev as a condition for clearance at least hints at the possibility that Chinese merger control will become more active than it has been in the past. Since merger control began in 2003 in China, most merger cases have been cleared without conditions and no case has been rejected outright. InBev is one of only a few cases where MOFCOM has imposed restrictions, and it is the most recent and only published case.²² It is not advisable to read too much into any one case, but the fact that MOFCOM chose to impose conditions to address a prospective concern suggests that companies applying for merger clearance would be well-advised to consider the range of issues that MOFCOM might raise.

These are the tentative lessons we draw from the InBev Decision. The merger control process in China is, of course, still in its formative stages, and future cases and policy creation by MOFCOM will be extremely important in further developing China's merger control policy.

²¹ Statement of Simon Pritchard, OFT Senior Director of Mergers, OFT Press Releases, November 18, 2008, available at <http://www.of.gov.uk/news/press/2008/134-08>.

²² The other decisions were issued prior to the AML and are not published.