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Return of the Tied House? The Problems of Domination by Large Companies

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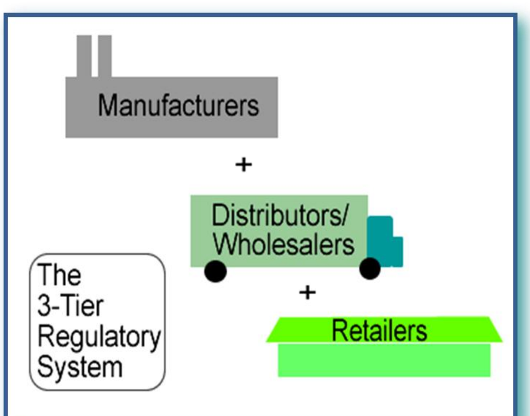
Before Prohibition, the alcohol market was dominated by large national companies that owned or had exclusive business deals with retailers. The retailers were called "Tied Houses" because they only sold one company's product. That lead to an increase in bars in local markets since each bar only sold one company's products. The national alcohol companies pushed hard on the retailer to make as much money as possible through whatever means they could. Local markets were flooded with cheap alcohol and aggressive sales. The resulting alcohol problems were so severe that they led to the equally severe solution of Prohibition.

Those who designed our alcohol regulatory system were very focused on preventing the kind of market domination where the manufacturer and retailers are tied through ownership, financial arrangements or special favors. As a result, they developed a three-tier system whereby each tier is separately licensed. Many states also require that each tier be independently owned. All of this is designed to prevent the domination of local markets.



A recent proposal to merge Anheuser-Busch InBev with SABMiller raises some of these concerns. This merger would combine the world's two largest beer companies. While the merger will likely involve selling off some assets to appease anti-trust regulators, it still would create a company with greater economic power and influence. It is even hard to predict how such a powerful company could impact our communities. But here are some things to watch:

1. <u>Domination of the distribution tier</u>

You may be surprised to know that in 2014, Beer Business Daily listed Anheuser-Busch (AB) as the US's largest beer distributor selling 135 million cases. Despite our three tier system, some states allow a manufacturer to own a distributor. AB has expressed an interest in owning a larger number of distributors and has recently purchased several in Colorado, California and Oregon.

In most states, distributors are independently owned but usually sell either AB or SABMiller products, but not both. Nevertheless, many have added local and regional craft beer to their product line. The reason is that craft products are experiencing increased sales, while pale lagers, such as Budweiser and Miller Lite, are lagging.

Craft beer companies and others have raised concerns about a new AB incentive program for distributors which could limit market access for small craft operators. According to an article in the Wall Street Journal, that program would provide "annual reimbursements of as much as $1.5 million if 98% of the beers they sell are AB brands." That program would leave little room for any other company's product.

2. Use of a large company's economic power to offer incentives and price reductions to squeeze out the competition.

A large company can offer products to a retailer at much lower prices than competitors due to their volume. In addition, many large alcohol companies offer a portfolio of different brands, not just their company branded products. This includes craft products acquired through mergers and craft-like products produced by the company. This scenario could produce a "Virtual Tied House." If the retailer buys the whole portfolio, they can meet the taste preferences of a variety of customers, they will likely get favorable pricing and will only have to deal with one company. After all, there is a limit to tap handles and shelf space and the full portfolio of a large beer company could simply monopolize it. This would reduce the ability of local craft companies to get products in stores, bars and restaurants.

If one company is successful in tying distributors and retailers in these ways, other companies will do the same. Then we could have a scenario similar to the historical Tied House system where hyper competitive markets flooded communities with cheap alcohol. To get good prices, retailers had to buy more product than they could sell causing them to dump cheap alcohol onto the market or use drastically reduced prices to juice up sales.

This scenario would not bode well for our local communities because greater alcohol sales invariably mean increased social problems. It also would not bode well for our local craft brewers who would have trouble getting their products to market. Enforcement of our alcohol regulations—particularly those involving fair trade practices—can help prevent the problems of local market domination. They focus on fairness and provide a more level playing field for all businesses, large or small.

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For more information, see www.healthyalcoholmarket.com
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