Brown Shoe Co. v. United States

370 U.S. 294 (1962)

Mr. Chief Justice WARREN delivered the opinion of the Court.

I.

This suit was initiated in November 1955 when the Government filed a civil action . . . alleging that a contemplated merger between the G. R. Kinney Company, Inc. (Kinney) and the Brown Shoe Company, Inc. (Brown), through an exchange of Kinney for Brown stock, would violate § 7 of the Clayton Act. The Act, as amended, provides in pertinent part [that no corporation shall acquire another entity, including partial acquisition assets and equity, where] "the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly."

A motion by the Government for a preliminary injunction . . . was denied, and the companies were permitted to merge provided, however, that their businesses be operated separately and that their assets be kept separately identifiable. The merger was then effected on May 1, 1956.

[When the government filed the complaint, Brown was] the third largest seller of shoes by dollar volume in the United States, a leading manufacturer of men's, Women's, and children's shoes, and a retailer with over 1,230 owned, operated or controlled retail outlets.[1] Kinney [was] the eighth largest company, by dollar volume, among those primarily engaged in selling shoes, itself a large manufacturer of shoes, and a retailer with over 350 retail outlets.

[The government alleged that the merger might substantially lessen competition or tend to create a monopoly] by eliminating actual or potential competition in the production of shoes for the national wholesale shoe market and in the sale of shoes at retail in the Nation. [Because the merger would foreclose] competition from a market represented by Kinney's retail outlets, [and would enhance] Brown's competitive advantage over other producers, distributors and sellers of shoes.

The Government argued that the 'line of commerce' affected by this merger is 'footwear,' or alternatively, that the 'line(s)' are 'men's,' 'women's,' and 'children's' shoes, separately considered, and that the 'section of the country,' within which the anticompetitive effect of the merger is to be judged, is the Nation as a whole, or alternatively, each separate city or city and its immediate surrounding area in which the parties sell shoes at retail.

. . . Brown . . . contended that, both at the manufacturing level and at the retail level, the shoe industry enjoyed healthy competition and that the vigor of this competition would not, in any event, be diminished by the proposed merger because Kinney manufactured less than 0.5% and retailed less than 2% of the Nation's shoes.

The Industry.

The District Court found that although domestic shoe production was scattered among a large number of manufacturers, a small number of large companies occupied a commanding position. Thus, while the 24 largest manufacturers produced about 35% of the Nation's shoes, the top 4—

[1] Of these over 1,230 outlets under Brown's control at the time of the filing of the complaint, Brown owned and operated over 470, while over 570 were independently owned stores operating under the Brown 'Franchise Program' and over 190 were independently owned outlets operating under the 'Wohl Plan.' A store operating under [any of these programs] agrees not to carry competing lines of shoes of other manufacturers in return for certain aid from Brown. . . .

International, Endicott-Johnson, Brown (including Kinney) and General Shoe—alone produced approximately 23% of the Nation's shoes or 65% of the production of the top 24.

In 1955, domestic production of nonrubber shoes was 509.2 million pairs, of which about 103.6 million pairs were men's shoes, about 271 million pairs were women's shoes, and about 134.6 million pairs were children's shoes. The District Court found that men's, women's, and children's shoes are normally produced in separate factories.

The public buys these shoes through about 70,000 retail outlets, only 22,000 of which, however, derive 50% or more of their gross receipts from the sale of shoes and are classified as 'shoe stores' by the Census Bureau. These 22,000 shoe stores were found generally to sell (1) men's shoes only, (2) women's shoes only, (3) women's and children's shoes, or (4) men's, women's, and children's shoes.

The District Court found a 'definite trend' among shoe manufacturers to acquire retail outlets. [Within this trend], between 1950 and 1956, nine independent shoe store chains, operating 1,114 retail shoe stores, were found to have become subsidiaries of these large firms and to have ceased their independent operations.

[The District Court also found that vertically integrated retailers typically sell shoes of the parent company], thereby foreclosing other manufacturers from effectively competing for the retail accounts. Manufacturer-dominated stores were found to be 'drying up' the available outlets for independent producers.

Another 'definite trend' found to exist in the shoe industry was a decrease in the number of plants manufacturing shoes. And there appears to have been a concomitant decrease in the number of firms manufacturing shoes. In 1947, there were 1,077 independent manufacturers of shoes, but by 1954 their number had decreased about 10% to 970.

Brown Shoe.

Brown Shoe was found [to be] a moving factor in these industry trends. Although Brown had experimented several times with operating its own retail outlets, by 1945 it had disposed of them all. However, in 1951, Brown [returned to retail and has acquired several small and large retailers. The acquired retailers considerably increased their sales of the Brown brand, although the continued selling other brands. Additionally, in the early 1950s], Brown also acquired the stock or assets of seven companies engaged solely in shoe manufacturing. As a result, in 1955, Brown was the fourth largest shoe manufacturer in the country, producing about 25.6 million pairs of shoes or about 4% of the Nation's total footwear production.

Kinney.

Kinney is principally engaged in operating the largest family-style shoe store chain in the United States. At the time of trial, Kinney [operated] over 400 such stores in more than 270 cities. These stores were found to make about 1.2% of all national retail shoe sales by dollar volume. . . .

In addition to this extensive retail activity, Kinney owned and operated four plants which manufactured men's, women's, and children's shoes and whose combined output was 0.5% of the national shoe production in 1955, making Kinney the twelfth largest shoe manufacturer in the United States.

Kinney stores were found to obtain about 20% of their shoes from Kinney's own manufacturing plants. At the time of the merger, Kinney bought no shoes from Brown; however, . . .

by 1957, [Brown became] the largest outside supplier of Kinney's shoes, supplying 7.9% of all Kinney's needs.

It is in this setting that the merger was considered and held to violate § 7 of the Clayton Act. . . .

III.

LEGISLATIVE HISTORY.

This case is one of the first to come before us [after Congress amended § 7 in 1950]. The amendments adopted in 1950 culminated extensive efforts over a number of years, on the parts of both the Federal Trade Commission and some members of Congress, to secure revision of a section of the antitrust laws considered by many observers to be ineffective in its then existing form. . . .

As enacted in 1914, § 7 of the original Clayton Act prohibited the acquisition by one corporation of the stock of another corporation when such acquisition would result in a substantial lessening of competition between the acquiring and the acquired companies, or tend to create a monopoly in any line of commerce.

The Act did not, by its explicit terms, or as construed by this Court, bar the acquisition by one corporation of the assets of another. Nor did it appear to preclude the acquisition of stock in any corporation other than a direct competitor. . . .

The dominant theme pervading congressional consideration of the 1950 amendments was a fear of what was considered to be a rising tide of economic concentration in the American economy. . . . Other considerations cited in support of the bill were the desirability of retaining 'local control' over industry and the protection of small businesses. . . .

First, there is no doubt that Congress did wish to 'plug the loophole' and to include within the coverage of the Act the acquisition of assets no less than the acquisition of stock.

Second, by the deletion of the 'acquiring-acquired' language in the original text, it hoped to make plain that § 7 applied not only to mergers between actual competitors, but also to vertical and conglomerate mergers whose effect may tend to lessen competition in any line of commerce in any section of the country.

Third, [to address the] rising tide of economic concentration, [Congress granted authority to block mergers] at a time when the trend to a lessening of competition in a line of commerce was still in its incipiency. Congress saw the process of concentration in American business as a dynamic force; it sought to assure the Federal Trade Commission and the courts the power to brake this force at its outset and before it gathered momentum. . . .

Fifth, at the same time that it sought to create an effective tool for preventing all mergers having demonstrable anti-competitive effects, Congress recognized the stimulation to competition that might flow from particular mergers. [Examples of such mergers include] a merger between two small companies to enable the combination to compete more effectively with larger corporations dominating the relevant market; . . . a merger between a corporation which is financially healthy and a failing one which no longer can be a vital competitive factor in the market.

Taken as a whole, the legislative history illuminates congressional concern with the protection of competition, not competitors, and its desire to restrain mergers only to the extent that such combinations may tend to lessen competition.

Sixth, Congress neither adopted nor rejected specifically any particular tests for measuring the relevant markets. . . . Nor did it adopt a definition of the word 'substantially,' whether in quantitative terms of sales or assets or market shares or in designated qualitative terms, by which a merger's effects on competition were to be measured.

Seventh, . . . Congress indicated plainly that a merger had to be functionally viewed, in the context of its particular industry. . . .

IV.

THE VERTICAL ASPECTS OF THE MERGER

Economic arrangements between companies standing in a supplier-customer relationship are characterized as 'vertical.' The primary vice of a vertical merger or other arrangement tying a customer to a supplier is that, by foreclosing the competitors of either party from a segment of the market otherwise open to them, the arrangement may act as a 'clog on competition,' *Standard Oil Co. of California v. United States*, 337 U.S. 293 (1949), which deprives rivals of a fair opportunity to compete. Every extended vertical arrangement by its very nature, for at least a time, denies competitors of the supplier the opportunity to compete for part or all of the trade of the customer-party to the vertical arrangement. However, the Clayton Act does not render unlawful all such vertical arrangements, but forbids only those whose effect 'may be substantially to lessen competition, or to tend to create a monopoly.' . . . Thus, determination of the relevant market is a necessary predicate to a finding of a violation of the Clayton Act because the threatened monopoly must be one which will substantially lessen competition 'within the area of effective competition' 'in any line of commerce in any section of the country.' Substantiality can be determined only in terms of the market affected.

The 'area of effective competition' must be determined by reference to a product market (the 'line of commerce') and a geographic market (the 'section of the country').

The Product Market.

The outer boundaries of a product market are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it. However, within this broad market, well-defined submarkets may exist which, in themselves, constitute product markets for antitrust purposes. The boundaries of such a submarket may be determined by examining such practical indicia as industry or public recognition of the submarket as a separate economic entity, the product's peculiar characteristics and uses, unique production facilities, distinct customers, distinct prices, sensitivity to price changes, and specialized vendors.

Because § 7 of the Clayton Act prohibits any merger which may substantially lessen competition 'in any line of commerce' (emphasis supplied), it is necessary to examine the effects of a merger in each such economically significant submarket to determine if there is a reasonable probability that the merger will substantially lessen competition. If such a probability is found to exist, the merger is proscribed.

Applying these considerations to the present case, we conclude that the record supports the District Court's finding that the relevant lines of commerce are men's, women's, and children's shoes. These product lines are recognized by the public; each line is manufactured in separate plants; each has characteristics peculiar to itself rendering it generally noncompetitive with the others; and each is, of course, directed toward a distinct class of customers.

Appellant, however, contends that the District Court's definitions fail to recognize sufficiently 'price/quality' and 'age/sex' distinctions in shoes. . . . [Specifically, Brown is critical of] the District Court's finding that children's shoes constituted a single line of commerce. Brown argues, for example, that 'a little boy does not wear a little girl's black patent leather pump' and that '(a) male baby cannot wear a growing boy's shoes.' Thus, Brown argues that infants and babies shoes, misses, youths, and boys shoes should each have been considered a separate line of commerce.

Assuming, arguendo, that little boys' shoes, for example, do have sufficient peculiar characteristics to constitute one of the markets to be used in analyzing the effects of this merger, we do not think that in this case the District Court was required to employ finer 'age/sex' distinctions then those recognized by its classifications of 'men's,' 'women's,' and 'children's' shoes. Further division does not aid us in analyzing the effects of this merger.

Brown manufactures about the same percentage of the Nation's children's shoes (5.8%) as it does of the Nation's youths' and boys' shoes (6.5%), of the Nation's misses' and children's shoes (6.0%) and of the Nation's infants' and babies' shoes (4.9%). Similarly, Kinney sells about the same percentage of the Nation's children's shoes (2%) as it does of the Nation's youths' and boys' shoes (3.1%), of the Nation's misses' and children's shoes (1.9%), and of the Nation's infants' and babies' shoes (1.5%). Appellant can point to no advantage it would enjoy were finer divisions than those chosen by the District Court employed. . . . We, therefore, agree with the District Court's conclusion that in the setting of this case to subdivide the shoe market further on the basis of 'age/sex' distinctions would be 'impractical' and 'unwarranted.'

The Geographic Market.

We agree with the parties and the District Court that insofar as the vertical aspect of this merger is concerned, the relevant geographic market is the entire Nation. . . .

The Probable Effect of the Merger.

Once the area of effective competition affected by a vertical arrangement has been defined, an analysis must be made to determine if the effect of the arrangement 'may be substantially to lessen competition, or to tend to create a monopoly' in this market.

[In this case], the foreclosure is neither of monopoly nor de minimis proportions, the percentage of the market foreclosed by the vertical arrangement cannot itself be decisive. In such cases, it becomes necessary to undertake an examination of various economic and historical factors in order to determine whether the arrangement under review is of the type Congress sought to proscribe. . . .

The present merger involved neither small companies nor failing companies. In 1955, the date of this merger, Brown was the fourth largest manufacturer in the shoe industry with sales of approximately 26 million pairs of shoes and assets of over $72,000,000 while Kinney had sales of about 8 million pairs of shoes and assets of about $18,000,000. Not only was Brown one of the leading manufacturers of men's, women's, and children's shoes, but Kinney, with over 350 retail outlets, owned and operated the largest independent chain of family shoe stores in the Nation. Thus, in this industry, no merger between a manufacturer and an independent retailer could involve a larger potential market foreclosure. Moreover, it is apparent both from past behavior of Brown and from the testimony of Brown's President, that Brown would use its ownership of Kinney to force Brown shoes into Kinney stores. . . .

Another important factor to consider is the trend toward concentration in the industry. . . . The existence of a trend toward vertical integration, which the District Court found, is well substantiated by the record. Moreover, the court found a tendency of the acquiring manufacturers to become increasingly important sources of supply for their acquired outlets. The necessary corollary of these trends is the foreclosure of independent manufacturers from markets otherwise open to them. And because these trends are not the product of accident but are rather the result of deliberate policies of Brown and other leading shoe manufacturers, account must be taken of these facts in order to predict the probable future consequences of this merger. It is against this background of continuing concentration that the present merger must be viewed.

Brown argues, however, that the shoe industry is at present composed of a large number of manufacturers and retailers, and that the industry is dynamically competitive. But remaining vigor cannot immunize a merger if the trend in that industry is toward oligopoly. . . .

Moreover, . . . not only must we consider the probable effects of the merger upon the economics of the particular markets affected but also we must consider its probable effects upon the economic way of life sought to be preserved by Congress. Congress was desirous of preventing the formation of further oligopolies with their attendant adverse effects upon local control of industry and upon small business. Where an industry was composed of numerous independent units, Congress appeared anxious to preserve this structure. . . . [T]he shoe industry is being subjected to just such a cumulative series of vertical mergers which, if left unchecked, will be likely 'substantially to lessen competition.' . . .

V.

THE HORIZONTAL ASPECTS OF THE MERGER.

An economic arrangement between companies performing similar functions in the production or sale of comparable goods or services is characterized as 'horizontal.' . . .

The Product Market.

Shoes are sold in the United States in retail shoe stores and in shoe departments of general stores. These outlets sell: (1) men's shoes, (2) women's shoes, (3) women's or children's shoes, or (4) men's, women's or children's shoes. Prior to the merger, both Brown and Kinney sold their shoes in competition with one another through the enumerated kinds of outlets characteristic of the industry.

The Geographic Market.

. . . The District Court found that the effects of this aspect of the merger must be analyzed in every city with a population exceeding 10,000 and its immediate contiguous surrounding territory in which both Brown and Kinney sold shoes at retail through stores they either owned or controlled. . . . [The record supports this conclusion]. . .

The Probable Effect of the Merger.

[The District Court found] that as a result of the merger competition in the retailing of men's, women's and children's shoes may be lessened substantially in those cities in which both Brown and Kinney stores are located. . . . Brown objects that the District Court did not examine the competitive picture in each line of commerce and each section of the country it had defined as appropriate. . . . While it is true that the court concentrated its attention on the structure of competition in the city in which it sat and as to which detailed evidence was most readily available, it also heard witnesses from no less than 40 other cities in which the parties to the merger operated. The court was careful to point out that it was on the basis of all the evidence that it reached its conclusions concerning the boundaries of the relevant markets and the merger's effects on competition within them. . . .

During 1955 in 32 separate cities, ranging in size and location from Topeka, Kansas, to Batavia, New York, and Hobbs, New Mexico, the combined share of Brown and Kinney sales of women's shoes (by unit volume) exceeded 20%. In 31 cities . . . the combined share of children's shoes sales exceeded 20. . . . [I]n 6 cities their share exceeded 40%. In Dodge City, Kansas, their combined share of the market for women's shoes was over 57%; their share of the children's shoe market in that city was 49%. In the 7 cities in which Brown's and Kinney's combined shares of the market for women's shoes were greatest (ranging from 33% to 57%) each of the parties alone, prior to the merger, had captured substantial portions of those markets (ranging from 13% to 34%); the merger intensified this existing concentration. In 118 separate cities the combined shares of the market of Brown and Kinney in the sale of one of the relevant lines of commerce exceeded 5%. In 47 cities, their share exceeded 5% in all three lines.

. . . In an industry as fragmented as shoe retailing, the control of substantial shares of the trade in a city may have important effects on competition. If a merger achieving 5% control were now approved, we might be required to approve future merger efforts by Brown's competitors seeking similar market shares. The oligopoly Congress sought to avoid would then be furthered and it would be difficult to dissolve the combinations previously approved.

Furthermore, in this fragmented industry, even if the combination controls but a small share of a particular market, the fact that this share is held by a large national chain can adversely affect competition. Testimony in the record from numerous independent retailers, based on their actual experience in the market, demonstrates that a strong, national chain of stores can insulate selected outlets from the vagaries of competition in particular locations and that the large chains can set and alter styles in footwear to an extent that renders the independents unable to maintain competitive inventories.

A third significant aspect of this merger is that it creates a large national chain which is integrated with a manufacturing operation. The retail outlets of integrated companies, by eliminating wholesalers and by increasing the volume of purchases from the manufacturing division of the enterprise, can market their own brands at prices below those of competing independent retailers. Of course, some of the results of large integrated or chain operations are beneficial to consumers. Their expansion is not rendered unlawful by the mere fact that small independent stores may be adversely affected. It is competition, not competitors, which the Act protects. But we cannot fail to recognize Congress' desire to promote competition through the protection of viable, small, locally owned business. Congress appreciated that occasional higher costs and prices might result from the maintenance of fragmented industries and markets. It resolved these competing considerations in favor of decentralization. We must give effect to that decision.

. . . We hold that the District Court was correct in concluding that this merger may tend to lessen competition substantially in the retail sale of men's, women's, and children's shoes in the overwhelming majority of those cities and their environs in which both Brown and Kinney sell through owned or controlled outlets. The judgment is affirmed.

Affirmed.