

KELLOGG: *Kellogg's Corn Flakes*, fortified with vitamin D by 1941, increased to 100% MDR, 1956 (Tr. 29,716-17; CX-K 457); *Pep*, fortified with vitamins D and B1 by 1941 (Tr. 29,715-17); *Special K*, fortified [147]with seven vitamins and protein, 1956 (Tr. 29,716, 29,948; CX-GM 564C); *Concentrate*, vitamin fortified and protein enriched, 1958 (Tr. 29,716); *40% Bran Flakes*, fortified with 100% iron, 1966 (CX-K 487); *Product 19*, fortified with 100% MDR of eight vitamins and iron, 1967 (Tr. 29,663); *Sugar Smacks*, fortified with $\frac{1}{3}$ MDR of vitamins and iron, 1967 (CX-K 7135S, 7352B, C); *Mini-Wheats* fortified with $\frac{1}{3}$ MDR of vitamins and iron, 1969 (Tr. 11,786-87; CX-K 533); *Raisin Bran*, fortified with 100% iron by 1969 (CX-K 415, 7177F).

GENERAL MILLS: *Hi-Pro*, fortified with seven vitamins and iron, 1958 (GMX 180); *Total*, fortified with 100% MDR of eight vitamins, 1961 (GMX 179B); *Corn Total*, fortified with 100% MDR of eight vitamins, 1966 (GMX 180B); *Vital 7*, vitamin fortified, 1967 (Tr. 17,162); *Alive*, fortified with extra Vitamin B2, Niacin and Iron, 1968 (Tr. 16,979; GMX 181B); *Kaboom*, fortified with 100% MDR of eight vitamins and iron, 1969 (CX-K 765E; GMX 174B); *Buc Wheats*, fortified with $\frac{1}{3}$ MDR of eight vitamins, as test marketed August 1970 (CX-K 765E; GMX 179B).

GENERAL FOODS: *Bran Flakes*, fortified with iron, 1966 (CX-K 487); *Fortified Oat Flakes*, fortified with six vitamins and minerals, 1967 (Tr. 37,052, 37,059; CX-GF 1406C); *Sugar Crisp*, fortified with $\frac{1}{3}$ MDR of vitamins and minerals, 1967 (Tr. 37,052); *Alpha Bits*, vitamin fortified to $\frac{1}{3}$ MDR, 1969 (CX-GF 601H); *Honeycomb*, vitamin fortified to $\frac{1}{3}$ MDR, 1969 (CX-GF 601H).

QUAKER: *Quisp* and *Quake*, fortified with $\frac{1}{3}$ MDR of vitamins and iron, 1968 (Tr. 15,044-45); *King Vitaman*, fortified with 100% MDR of vitamins and iron, 1970 (CX-K 765C).

501. In 1970, vitamin fortified brands accounted for some 17% of industry pound sales, and cereals fortified with iron accounted for another 6% of the market (CX 434). Respondents' fortification efforts prior to 1970 achieved competitive results—for example, the competitive impact of Kellogg's Product 19 on General Mills' Total (CX-K 7176A; CX-GM 567A), the fortification rivalry between Kellogg's Product 19 and Special K and General Foods' Fortified Oat Flakes (CX-GF 34A), and between General Foods' Sugar Crisp and Kellogg's Sugar Smacks (CX-K 595A, 7352B, C, I).

502. This fortification activity prior to 1970 took place not only in the climate of the pronouncements of the Council on Foods and Nutrition of the American Medical Association and the Food and

Nutrition Board of the National Research Council, related above (Finding 493), but also in the face of an adverse position taken by the Food and Drug Administration (FDA).

503. FDA policy adverse to the fortification of RTE cereal products was a major obstacle to RTE cereal fortification. During [148]the mid-1960's, the FDA publicly opposed fortifying RTE cereals beyond allowable limits, on the ground that the availability of vitamins to consumers from other sources made cereal fortification unnecessary (Tr. 29,949-50, 37,054-59).

504. In 1962, the FDA commenced rulemaking proceedings concerning regulation of processed food fortification (27 Fed. Reg. 5815 (June 20, 1962)). In 1966, it proposed a rule, Part 80.2 of which would have prohibited the addition to RTE cereals of vitamins and minerals other than niacin, thiamin, riboflavin and iron. Minimum and maximum limits covering the use of these four nutrients would also have been established (31 Fed. Reg. 8525-26 (June 18, 1966)) (KX 101; Tr. 29,718, 37,056). Part 80.2 embodied the prevailing FDA policy that restoration of vitamins to whole-grain levels constituted the maximum appropriate vitamin supplementation (Tr. 37,056). FDA held protracted hearings regarding the proposed regulation (Tr. 29,718; CX-CI 80A).

505. If adopted, the FDA regulation would have precluded the high levels of fortification subsequently adopted by respondents in 1971-1972, and would have required the reformulation of certain established fortified cereals (KX 101; *see, e.g.*, GMX 174 through 181; CX-GF 102K).

506. At the time of the FDA's rule proposal, respondents anticipated serious impact on their fortified cereals (Tr. 29,949). For example, in 1966, General Mills believed that the regulation threatened the future of its fortified Total: "[T]he probability of passage creates a serious potential threat to the brand" (CX-GM 564C). General Mills' 1969-1970 Total marketing plan stated: "Possible future FDA regulations could force elimination or massive reformulation of Total" (CX-GM 567A). Kellogg delayed increasing the iron content of Raisin Bran from 80% to 100% MDR until after it was advised that such action would not cause a government reprimand (CX-K 439B).

507. The effect of the FDA policy was to delay fortification of many cereals until the 1970's (Tr. 13,141, 29,717-19, 35,812, 37,053-55).

508. In addition to the FDA, American Medical Association and National Research Council opposition to fortification of foods and perhaps as a result of such opposition, there was limited consumer

demand for fortified RTE cereals during the 1960's and only limited, temporary success for products that were fortified (CX-GF 102G; CX-K 487; Tr. 15,043-44, 16,980-82). The record fails to indicate that respondents' individual competitive efforts prior to 1970 in the field of product fortification were not fully commensurate with the public demand. There is no evidence that indicates that respondents reached agreements concerning, or coordinated, their pre-1970 fortification conduct.

509. Throughout the pre-1970 period and thereafter, respondents individually engaged in extensive research to overcome technical [149]problems involved in cereal fortification. There have been many such problems including workable methods of fortification application, uniformity of product, unacceptable taste, odors and appearance, deleterious chemical reactions, maintenance of vitamin potency through the cereal processing procedure, maintenance of proper product moisture levels and shortened shelf life. These problems varied product by product and by the particular nutrient and combination of nutrients involved (Tr. 12,367, 13,004, 13,339-401, 13,670-71, 13,668-69, 14,150, 16,982, 29,280-82, 29,951, 32,911, 32,916-17, 35,808, 36,670-71, 37,002, 37,052-53, 37,062-63; GMX 373).

510. Some of the problems have been very difficult to overcome. For example, General Mills has never been able to add vitamins A and D to Cocoa Puffs or to add minerals other than iron to any cereals because of bad taste problem (Tr. 35,803, 35,813). Considerable expenses were incurred in researching and implementing product fortification (Tr. 16,982, 29,952-53; CX-GF 477).

511. General Foods' research into beneficial product additives was not limited to vitamin and mineral fortification. Starting about the end of 1959, General Foods promoted research on the possible inclusion of phosphates to inhibit dental caries. Much of this was done in conjunction with the Indiana University Foundation, as well as outside specialists and statisticians. Because of what appeared to be questionable research procedures, Indiana University and General Foods agreed to terminate the joint research arrangement in 1972. General Foods continues to perform animal research with phosphates (Tr. 37,110-11).

512. General Foods' unilateral investment of substantial sums in research into the prevention of tooth decay is inconsistent with complaint counsel's allegation that General Foods, in conjunction with other respondents, avoided having one respondent acquire a competitive advantage over the others. Respondents' overall, vigorous competition in the introduction of new products (*infra*, Findings

530-602) is also totally inconsistent with the charge that they conspired in the particular area of fortification.

513. In the late 1960's and early 1970's, there was a dramatic change in the national attitude toward the fortification of cereals. During 1969, the President had convened a White House Conference on Nutrition, which issued a report in December 1969 (GMX 501). That report was to the effect that there were significant nutritional deficiencies in the diets of large segments of the population. It was recommended that the proposed FDA regulations barring the fortification of breakfast cereals not be adopted, because the widespread acceptance and consumption of breakfast cereals made them effective carriers of essential nutrients. It attacked the view that all needed nutrients were obtained from ordinary diets and recommended strong food fortification programs (Tr. 35,811-12; GMX 501Z94-96, Z120-22, Z-253). Consequently, the FDA abandoned its proposed rule to prohibit food fortification (Tr. 29,718, 37,057-58). [150]

514. The Conference increased consumer interest in vitamin fortification and provided impetus to the fortification programs of each respondent, which resulted in whole-line fortification in the early 1970's (Tr. 13,140, 29,719-20, 35,057-08, 35,810-11).

515. At the time of the White House Conference, congressional hearings were being held, but there was no resolution of the matter at that time (Tr. 37,058).

516. Subsequently, in July 1970, Mr. Robert B. Choate, a civil engineer, in testimony before a congressional committee, criticized the lack of nutrients in RTE cereals. Mr. Choate's testimony further increased industry and consumer interest in vitamin fortification. His testimony was widely publicized, and the majority of RTE cereal consumers were aware of it (Tr. 37,061-62; CX-GF 3000Z-105).

517. Choate rated RTE cereals by name as to their nutritional value. As a result, certain fortified brands benefited from Choate's highly publicized testimony (Tr. 29,951-52). Sales of four fortified cereals, Fortified Oak Flakes, Total, Special K and Product 19, improved after Choate testified (CX-GF 477C, 1429B; KX 4; CX-GF 340A). Purchase of certain nonfortified cereal brands, Wheaties, Cheerios, Rice Krispies, and Grape Nuts, appeared to decline (CX-GF 1429B; see CX-GM 16A, 17A).

518. Kellogg had commenced development of the systems necessary for extending fortification at the one-third MDR level to all of its cereals in the late 1960's, at which time Kellogg had decided to fortify all products (Tr. 29,278-81). Kellogg, at the time of Choate's testimony, had already begun to install the equipment required to

apply increased levels of eight vitamins called for in its expanded fortification effort. This enabled it to begin production of cereals fortified at the new, higher vitamin levels within several months of Choate's testimony (Tr. 29,952-53; see CX-K 7187R). Kellogg's decision to fortify its entire line was given additional impetus by the 1969 White House Conference on nutrition (Tr. 29,719-20). The decision had already been made to fully fortify prior to Choate's testimony (Tr. 29,719-20).

519. Kellogg's Sugar Pops, Froot Loops, Apple Jacks, Sugar Frosted Flakes, Cocoa Krispies and Puffa Puffa Rice were fortified by late 1970 or early 1971 (CX-K 7187R). Two of Kellogg's largest selling brands, Corn Flakes and Rice Krispies, were not fortified until 1972; Corn Flakes was not fortified until September of that year (CX-K 7192F, 7193G, 7209E).

520. General Mills decided to fortify all its cereals to the $\frac{1}{3}$ MDR level of seven vitamins and iron on September 17, 1970 (Tr. 35,814; GMX 373). It fortified the majority of its cereals from August 1971 to January 1971 (GMX 174 thru 182). Fortification of Cheerios and Wheaties was in August 1971, and General Mills' established presweetened cereals were fortified from October 28, 1971, to January 1972 (GMX 174, 175, 177, 179). [151]

521. General Foods' decision to fortify its entire line of cereals preceded Choate's testimony (Tr. 37,052, 37,062). By February 1970, General Foods was prepared to fortify its entire line of cereals (at $\frac{1}{3}$ MDR vitamin and 100% MDR iron) subject to "Business Manager approval" (CX-GF 2022E). Choate served to accelerate implementation of General Foods' decision (Tr. 37,062). By late 1970 or early 1971, General Foods had completed its plan for such fortification and set a schedule to fortify its brands through 1971 and 1972 (CX-GF 477). General Foods planned to fortify its cereals in stages—first the presweets by September 1971, and then the remaining cereals by March 1972 (CX-GF 477C). The project was actually completed in 1971 (Tr. 37,059).

522. General Foods, through advertising and other promotional activity, attempted to secure a competitive advantage for its fortified products (CX-GF 340B, 477C). Kellogg recognized that it had been disadvantaged by General Foods having fortified its Raisin Bran before Kellogg did so (CX-K 7198D, E).

523. Kellogg introduced its newly fortified line of cereals in 1971 with an aggressive advertising and promotional campaign (CX-K 765R, S, U, W, Y, Z-2). However, since Kellogg had lagged behind its competition by not fortifying its most popular brand, Corn Flakes,

until September 1972, it lost sales to General Mills' Cheerios and Wheaties and to General Foods' Post Toasties (CX-K 7192F, 7209E).

524. The foregoing recitation of respondents' activities in the area of product fortification reveals that they were fully consistent with individual, competitive responses to stated public policy and consumer interest and demand.

Complaint counsel, however, assert (CPF 8-227 thru 8-233; CRPF 8-264 thru 8-269) that respondents convened meetings of the Executive Committee of the Cereal Institute on July 27, 1970, and August 21, 1970, in order to agree on how to respond to the attacks of Choate and others on the cereal industry for its failure to provide nutritious food, and that respondents there reached agreement on how to fortify their RTE cereals. This agreement is evidenced, according to complaint counsel, by the contemporaneous actions of respondents to fortify to the $\frac{1}{3}$ MDR level.

525. The July 27, 1970, meeting of the Executive Committee of the Cereal Institute was called "to consider the impact of the recent testimony of Robert Choate in which he attacked the nutritional value of cereals" and to decide upon "what action if any should be taken by the Institute on behalf of the industry to introduce proof of the nutritional value of cereals before the Subcommittee and otherwise to repair the damage done by the unjustified statements and charges of Mr. Choate" (CX-CI 78B). The only action taken at the meeting, that was evidenced, was that of authorizing the Institute to arrange for a [152]leading nutritionist to testify before the Senate subcommittee "as to the nutritional value of breakfast cereals and their place in the American diet" (CX-CI 78B).

526. On August 21, a special meeting of the Board of Directors of the Cereal Institute was held to discuss the testimony by Institute and industry witnesses which had been presented to the Senate subcommittee on August 4, and to discuss further efforts to educate the public on the role RTE cereals played in a nutritional diet (CX-CI 80). It was noted in the minutes of the meeting that Senator Moss of the Senate Subcommittee had suggested that the cereal industry should eliminate differences in the nutritional content of breakfast cereals and make greater progress in educating the public of nutritional facts concerning breakfast cereals; and that Mr. Paxton, the Cereal Institute's legal counsel, had advised that "despite the senator's suggestion, the elimination of product differences might not be an appropriate matter for concerted action" (CX-CI 80A).

527. The record contains no evidence that respondents discussed any plans for action regarding fortification at either of the two Cereal Institute meetings. Representatives of Kellogg and General

Mills who were present at the meetings testified that there were no agreements regarding fortification (Tr. 29,720-21, 35,463, 35,806, 35,815). And the record contains no evidence to overcome this testimony. Nor is there any evidence that the respondents otherwise communicated regarding their fortification activity, or that any respondent had advance knowledge of the fortification plans of the others. General Mills became aware of competitors' fortified products only when they appeared on retail shelves (Tr. 35,814).

528. Not all cereals were fortified to the $\frac{1}{3}$ MDR level (Tr. 29,663, 37,095; CX-K 765C). To the extent they were, this is not surprising inasmuch as breakfast is one of the three usual daily meals, and respondents were being responsive to recommendations of the White House Conference regarding fortification levels (GMX 501Z-101, Z-121, Z-197-98, Z-231, Z-232). General Mills was unaware of Kellogg's and General Foods' plans when it set fortification levels (Tr. 35,808, 35,814).

529. Complaint counsel do not challenge the right of respondents to belong to the Cereal Institute. The two meetings of the Institute, relied upon by complaint counsel for their hypothesis of agreement, have not been shown to have been conducted for other than legitimate purposes.⁴⁸ There is no basis for an inference that [153] fortification activities, which were most reasonable in the light of ongoing events, were in response to an otherwise unproved agreement rather than the ongoing events.

4. *Introduction of New Products*

Complaint counsel assert that there is a barrier to entry into the RTE cereal industry and would place responsibility for the existence of the barrier upon respondents. The cornerstone of the barrier to entry theory, which theory will be considered in the next section, has been termed by complaint counsel "brand proliferation." It is complaint counsel's position that respondent's avoidance of competition by other means led them to turn to brand proliferation, "the introduction of a large number of differentiated, highly advertised trademarked brands" (CPF 1-31, 9-1, 9-3, 9-35; CRPF 9-2, 9-10, 9-11).

530. Complaint counsel and their expert witnesses have conceded that respondent's brand proliferation is vigorously competitive, not predatory and not in itself unlawful (Tr. 22,607, 22,614-15, 22,622,

⁴⁸ The Cereal Institute was founded in 1941 for the purpose of advancing public understanding of the nutrition offered by cereal products (Tr. 11,863-72).

22,629, 22,865, 22,906, 23,264, 23,304, 23,678, 27,267; GFX 1166A-B, 1167).

531. Respondents engaged in unrestrained and uncoordinated competition in the introduction of new products. Such competition was intense (Tr. 21,922, 22,056, 22,605-08, 22,905-06, 22,615), and there is no evidence of a conspiracy or intent to deter entry by means of new product introductions (Tr. 22,109, 26,693, 27,028, 28,284, 30,518-23, 30,538).

532. Respondents, therefore, may not be held responsible for the results of this legitimate method of competition unless it was the proximate result of their having otherwise limited their competitive efforts as charged. However, as I have already held, complaint counsel have failed to prove those charges. Further, even if respondents had conspired or otherwise unlawfully coordinated their other competitive efforts, new product introduction would still have remained as a legitimate vehicle of competition. There is no causal relationship shown between the alleged avoidance of other kinds of competition and competition by brand introduction. Not only is there no showing of proximate cause, but, if respondents had conspired to fix prices or had engaged in price leadership-price followership in lieu of overt collusion, competition by introduction of a large number of differentiated products would have been avoided as the antithesis of such coordinated behavior (*see, supra*, findings 192-97).

As found above (Findings 229-31, 238-39, 245-47, 250-51, 323-26), respondents did not want to engage in price wars and the record does not evidence strong price competition among them. This is consistent with Professor Schumpeter's theory that firms in oligopolistically-[153]structured industries would tend to pursue competitive strategies which could not easily be matched by their rivals; that price competition, for example, would give way, among other things, to the development of new products, whereby a company could secure an extended competitive advantage (Tr. 38,276). As Dr. Scherer has written, *Industrial Market Structure and Economic Performance* 342 (1st ed. 1970):

[A]ny fool can match a price cut but an ingenious promotion campaign is hard to counteract.

This may well explain the emphasis by respondents on competition through new product introduction rather than price competition. But respondents may not be held accountable for any results flowing from their individual choice to pursue this lawful means of competition.

The following findings, therefore, are not necessary to my disposi-

tion of the issue of the introduction of new products, but are included for the use of a reviewing authority in the event it might take a different view.

533. Consumers desire variety for breakfast (Tr. 14,421, 14,446, 17,191, 17,398-401, 22,751, 35,367, 35,400, 35,447, 36,372; CX-CI 103Z-64; GFX 1153Z-71). Such a desire is responsible in large measure for the differentiation of RTE cereals (Tr. 22,751). A firm in the RTE cereal industry must introduce new products in order to remain profitable and compete for market share (Tr. 38,520, 38,797-98, 38,830; CX-CI 103Z-5).

534. Kellogg's policy has been to rely primarily on its proven brands, but to build on top of them with new products having good potential (CX-K 397D, 549C, 7358F). It believes that if it has a product with wide appeal, it must introduce it or someone else will; that it is better for Kellogg to continue to expand its products even if it is taking some business away from other Kellogg products than for a competitor to do so (Tr. 13,046-51, 29,954, 29,683-84).

535. "Although Kellogg does not agree that all profitable opportunities in the ready-to-eat cereal market have been exploited, Kellogg is doing its best to continue to exploit those additional opportunities . . ." (KPF 5-155).

536. General Mills stressed new product introduction at increasing levels as a major competitive effort and sought to outdo competitors in this regard (Tr. 17,353-66; CX-GM 38A, 608F, 609M, 610W). It believed it to be imperative to continue to introduce competitive new products (CX-GM 263A). General Mills was concerned at the inroads on its own absolute sales volume and market share that new products of its competitors might make (CX-GM 3D, E). Both General Foods and Kellogg recognized General Mills' policy of stressing new product introduction (CX-GF 4039Z-1; CX-K 553H).
[155]

537. General Foods also recognized a competitive requirement to introduce new products. As early as the 1950-1952 three-year plan for the Post Cereal Divisions, we find (CX-GF 167Z-10):

The need for new products which could augment our volume, help carry our overhead, and at least potentially contribute to profits has long been recognized. Since the total cereal business is at best stationary, and since therefore our principal chance to increase our volume is to take business away from competitors, new products are vitally important. It is not easy to increase the share of business done by our older established products.

538. General Foods, from the early 1960's, introduced new products in an attempt to maintain total volume and to make up for declining sales of established General Foods brands. New products

were also viewed as the key to growth (Tr. 14,140, 36,371; CX-GF 4A, 17D, 324A, 602K, 2044D, 4039Z-53).

539. General Foods, in 1967, decided to remain in the RTE cereal industry by placing a high priority on developing new products (CX-GF 4039D, G). In its proposed marketing plan for FY's 1968-1970, we find (CX-GF 4039Z-59):

The underlying assumption for Post new product strategy is that over the next three to five years continued competitive new product pressures, compiled with a static market will force volume losses on brands currently being marketed. . . .

* * * * *

Therefore, Post's new product program will be designed over the next three years to provide new products to hold or slightly grow total Post volume.

540. Changes in American society in the 1950's and 1960's, with resultant changes in consumer demand, contributed in large measure to the introduction of new RTE cereal products. The "baby boom" significantly affected the RTE cereal industry. Since RTE cereals are so convenient, the increase in the number of children offered a great opportunity for producers to develop new products to appear to them (Tr. 29,621-22, 29,786-87; CX-GM 736A). Because of the increased pace of modern living and the increased number of women in the labor force, there was an even greater demand for RTE cereals [156]which children could eat without parental assistance (Tr. 29,623-24, 29,787). Other shifts in demand, including the call for nutritious and natural cereals, also impelled respondents to introduce new products (Tr. 26,256, 29,680-84, 29,787).

541. The advent of television enabled respondents to visually impact consumers with the claimed benefits and attributes of new products. This ability to have a direct, nationwide impact on potential consumers facilitated the sale of new products and provided an incentive to respondents to develop new products (Tr. 27,100-01, 29,624, 29,702-07, 29,780-81; CX-GM 736A; CX-GF 4U; CX-K 563D).

542. New products were introduced by each respondent in order to compete against other RTE cereal manufacturers. Kellogg, for example, introduced a new product, Puffa Puffa Rice, so that it would not be preempted by a Quaker product, Tin Tin, that was being successfully marketed in Canada (Tr. 12,380-83, 12,891-92, 12,965-66, 22,131, 23,081-82, 30,706-07; CX-K 7163A). Kellogg introduced Product 19 to compete with General Mills' Total (Tr. 12,396-98, 12,839-40; CX-K 7353H), OK's to compete with General Mills' Cheerios, Froot Loops to compete with General Mills' Trix, and

Cocoa Krispies to compete with General Mills' Cocoa Puffs (Tr. 11,907-12, 12,684-94, 12,875-76, 13,545-46, 29,661-62; CX-K 502C). And Kellogg introduced its granola in response to entry into that segment by competitors (Tr. 13,087-88), as did General Mills (Tr. 17,802).

543. General Foods, during the early to mid 1960's, spent several million dollars to introduce a line of corn flakes with fruit (GFX 416D). It considered this to be a very exciting opportunity to secure a real competitive advantage, to the point of overtaking Kellogg (Tr. 36,380-81; GFX 1297). Even with respect to new products that were essentially variations of existing ones, General Foods sought to capture a small but profitable share of the total RTE cereal business (CX-GF 6T).

544. While respondents' new product introductions, to some extent, expanded the RTE cereal market by appealing to additional consumers and inducing consumers to eat more cereal products (CPF 9-286; Tr. 7573, 11,432, 13,010, 15,223-26, 17,681-82, 29,678-79, 29,780, 35,410, 35,417, 35,421-22; CX-K 560C; CX-GF 4039Z-53), they did have a competitive impact on respondents' other RTE cereal products, either by a reduction of sales or by adversely affecting sales growth (Tr. 7551, 7559-70, 8824-25, 14,198-99, 14,088-89, 14,220-27, 14,966, 15,222, 15,754-55; GMX 71, 73, 97, CX-K 397C; CX-GF 1455I).

545. Kellogg did not believe that every new product had to be profitable as long as the whole line showed a profit (CX-K 565I, L). Kellogg introduced new products when necessary to stop competitors from making inroads into Kellogg's business (Tr. 11,316; CX-K 686B). Kellogg believed that the introduction of two products at the same time reduced product trial (Tr. 12,965-70; CX-K 604A-C). Kellogg increased its advertising on Froot Loops while General Mills was [157]seeking to introduce Lucky Charms (Tr. 22,133-34). It also increased its advertising of Special K when General Foods introduced Fortified Oat Flakes (CX-GF 34).

546. General Mills introduced products with relatively low life potential in order to boost its overall line share of the market and counter a potential loss of customers to competitors' new products (CX-GM 3D, E). It introduced new brands as defensive moves to help prevent competitors' new brands from taking hold (CX-GM 2A, C, 262B, 276, 2171C, 2176F). It sought to keep its own products on the shelves, even though it recognized they had no future, until it could introduce still more of its own products to replace them (CX-GM 285). General Mills increased its advertising, use of coupons, and use

of samples with Total during Kellogg's introduction of Product 19 (Tr. 17,620-29, 23,075; CX-GM 21, 123A, B, 570N, Z-15, 720A).

547. General Foods introduces a new product only when it is believed to meet a perceived consumer demand and a reasonable profit can be anticipated (Tr. 36,372). It has never introduced a product that it did not think would succeed (Tr. 13,666, 36,435), although it did not expect its brand introductions in the 1960's to be as long lived as older brands (CX-GF 4039Z-59). It has introduced line extensions of particular cereals (e.g., flavor variations) to induce consumers to stay with its products rather than try RTE cereals of competitors (Tr. 17,481-82; CX-GF 1455C, 2029B).

548. Kellogg believed that the growth of sales in an area meant that there might be an opportunity for a new brand in that area. Its general practice, therefore, was to identify areas of opportunity for new brands by looking at the sales growth of particular brands in particular market areas (Tr. 12,832-41).⁴⁹

549. Kellogg has many sources for its new product ideas. These include brainstorming sessions involving Kellogg employees and members of its advertising agency (Tr. 29,977); outside consulting firms (Tr. 30,034); and observations of the marketplace (Tr. 16,534-35, 16,871-73, 29,795, 37,014-15, 37,030; GFX 1299). For example, Kellogg continually monitors the products of its competitors to determine whether an opportunity for an improved product exists (Tr. 12,269, 12,404, 29,801-02). Kellogg's General Sales Manager urged all Kellogg product marketing managers to watch for the product innovations of small manufacturers. He advised marketing managers to [158]"keep especially alert for successful locally marketed products that could be duplicated and mass-produced for national marketing—especially those compatible with our existing product lines" (CX-K 676B). Once such an idea was obtained, Kellogg, because of its technological capabilities, could improve on it and make the Kellogg product available nationwide (Tr. 12,184, 29,609-11).

550. Almost every department at Kellogg has some responsibility for the development of a new product, including the research and development group, the marketing research group, the process development, packaging development and quality control groups, the administrative group, the controllers and the purchasing people (Tr. 29,774, 37,032-33). The product development coordinator, whose position was established in 1958, is responsible for facilitating a

⁴⁹ For example, the growth of General Mills' Total led Kellogg to develop Product 19 (Tr. 29,795-96); Froot Loops were introduced to take advantage of an opportunity to appeal to users of the first fruit-flavored presweet, Trix, another General Mills product (Tr. 12,875-76).

product's orderly progression through its developmental stages into test market and general distribution (Tr. 29,773-75).

551. Kellogg made extensive use of marketing research tests to determine consumer reaction to various characteristics of products. This included blind paired comparison tests to determine what consumers deemed to be significant differences between products (Tr. 11,638-39, 12,957-62, 29,846). This was to prevent the offering of a me-too product (a product without a significant difference), which is recognized to be a likely failure in the marketplace (Tr. 9184-88, 12,965, 14,516-25, 14,584-86, 14,966-67, 15,228, 15,847, 15,851-53, 15,952, 17,453, 17,627-31, 17,634, 17,650, 22,722, 26,549; CX-K 396B).

552. Thus, the development of a new Kellogg product calls for expensive testing, including consumer panel tests, concept testing, blind paired comparison tests, in-home tests, central location tests, test marketing, as well as taste testings which expert respondent employees are continuously engaged in (Tr. 15,981-16,046, 29,800, 29,843-46, 32,970-82, 37,039-44).

553. Although each new product may vary as to the steps in development and problems encountered, Product 19 affords some perspective of what can be involved in the development of a new product (Tr. 29,794). Kellogg observed the success of General Mills' Total, as well as vitamin and mineral supplements like One-A-Day vitamin pills and Geritol. Kellogg analyzed and tested Total and decided that that product indicated an area of opportunity for Kellogg (Tr. 29,795-96).

554. Kellogg employees from all sections of the company then gathered to discuss the characteristics, technological needs, and competitive potential of the desired product. Upon establishment of a product objective, research personnel were put to work. They requisitioned the use of a pilot plant and laboratories for the manufacture of a product prototype. Once work on the product had begun, the group met constantly to review the prototype and its progressive transformations (Tr. 29,796-99). [159]

555. After the manufacture of what was believed to be a successful prototype, Kellogg employees conducted internal taste tests in which they compared the Kellogg product with Total. Generally, after a prototype has elicited positive responses from an internal taste panel, Kellogg turns it over to members of the process development department, the packaging department and the research department for further improvements. Meanwhile, Kellogg continues testing the product in order to insure consumer acceptance. If the results of these tests are encouraging, the company hires professional testing organizations to conduct panel tests among

consumers. Because the results of the new product's consumer tests were positive, Kellogg decided to go ahead with it, Product 19 (Tr. 29,800, 29,835-37, 29,846-48, 29,887-88).

556. Once Kellogg decided to market Product 19, its production required technology that had never been used under manufacturing conditions. In order to test this technology, Kellogg established a manufacturing pilot plant with actual-sized equipment, but on a smaller scale. This plant cost \$550,000.00. Product 19 was test marketed in 1966 throughout the Pacific West Coast, in Florida and in Texas. Although the product lost money during test marketing, Kellogg had expected the loss and considered it an investment (Tr. 29,848-52, 37,246-47; CX-K 7368B).

557. After being test marketed for 18 months, Product 19 proved to be a success. Kellogg then established a full-scale production facility which cost approximately \$4 million. This investment did not return any profits until Product 19's third year of production. It took seven years to recoup the product's early operating losses (Tr. 29,854-55, 29,858).

558. New product ideas at General Mills are generated from several sources, such as research and development, marketing research and interviews with consumers. New product ideas are first concept tested with consumers. A concept test is based on a pictorial representation and a written or oral description of the proposed new product. New product ideas which are well received by consumers are then guidance tested with consumers. Guidance testing is a sequence of tests in which groups of 50 to 75 consumers taste the product and respond to written questions concerning its attributes. The product is modified after testing in response to consumer input. A product that is rejected by consumers is not pursued. Products that survive guidance testing are then put through large scale evaluative testing. Here, the product is placed with a representative sample of 300 to 600 consumers to determine its level of satisfaction (Tr. 15,966-71, 15,978-79, 15,983-97, 15,999).

559. General Foods periodically analyzed the RTE cereal market by looking at segments of people and brands to try to find an unoccupied space or gap in the market. Brands were arrayed in relation to each other based on how people perceived them, and how they were rated with respect to particular attributes. People indicated what brand they would substitute if they could not find a [160] certain product. New product ideas were suggested by the study reports (Tr. 14,192-93, 14,407-16).

560. General Foods' market research department regularly conducted product testing, advertising research, information-gathering

on marketplace performance, test marketing research, attitude studies, packaging tests and other types of research (Tr. 14,344; *see, e.g.*, GFX 584).

561. The market research department also collected information about the types of people who were buying different products—"consumer profiles." Studies to learn what was happening in particular markets were also conducted (Tr. 14,345-46).

562. General Foods' and competitors' new products and their performance were evaluated (Tr. 14,346; GFX 552). Market Research conducted product quality tests in which consumers were asked to compare General Foods brands with other cereal products (Tr. 14,472-74; GFX 547, 549).

563. Information was secured from syndicated types of services, such as A.C. Nielsen Company, SAMI and MRCA and from market research organizations (*see, e.g.*, Tr. 14,349; GFX 289, 537, 547; CX-GF 1348).

564. General Foods' market research department thus was able to obtain information concerning the incidence of cereal purchases, the demography of the consumer groupings and the frequency of purchases (Tr. 14,365).

565. An effort was then made to come up with products that answered people's wants so identified and measured (Tr. 14,370).

566. Market research would track a new product's performance in terms of volume, share of market and consumer feedback. Such tracking would aid in the development of new product ideas (Tr. 14,368).

567. Consumer testing continued long after the introduction of a brand. General Foods tried to determine how its products were performing in the marketplace and to evaluate new opportunities (*see, e.g.*, GFX 535, 552).

568. New product ideas came from many sources—personal experience, marketing sources, marketplace sources, but primarily from technical sources (Tr. 37,015). Some ideas were generated in brainstorming sessions (*see, e.g.*, GFX 1299).

569. Following a brainstorming session, representatives from technical research, marketing research and marketing would meet to select those ideas which appeared to have merit (Tr. 37,032). [161]

570. These ideas would then be presented to potential consumers in an "omnibus test," for group discussion and evaluation. This is also known as "concept testing" (Tr. 14,417, 37,035, 37,037).

571. After omnibus testing, highly regarded product concepts would be considered for feasibility by technical personnel who would

develop prototype products reflecting particular ideas (Tr. 37,037, 37,223).

572. A prototype would be exposed to the consumer through market research. Research and development personnel would consider feedback and modify the product accordingly (Tr. 13,412).

573. Further consumer testing would be conducted, exposing prototype products to hundreds or even thousands of families for their reactions (Tr. 37,040).

574. If the product still looked promising, it would be test marketed to indicate what might be expected on a national scale (Tr. 36,440, 37,043).

575. If the product performed well in test market—if it appeared that its potential volume was sufficient to constitute a viable business—it would be introduced nationally. Not all products that were test marketed went into national distribution (Tr. 37,043–44).

576. Performance of a product in national distribution usually lagged behind performance in the test market. If a product failed to meet the goals set for it, it was withdrawn (Tr. 37,044–45).

577. Each product concept was evaluated several times as it was developed to determine whether it justified additional investment. Many concepts would be discarded; others would move forward toward the marketplace (Tr. 36,375–76).

578. General Foods had a New Product Committee, composed of senior managers in the RTE cereal business, to evaluate ideas and to decide whether they justified further investment (Tr. 36,375).

579. Utilization of excess capacity was one of the considerations in evaluating new product development opportunities (Tr. 13,481; GFX 423C).

580. Several of General Foods' new products were offshoots of products made by the Jersey Cereal Company, the small RTE cereal producer that General Foods had acquired (CX-GF 167Z-11).

581. In 1950, 26 brands were in distribution beyond test market. During the next 23 years, the largest six firms introduced 84 brands beyond test market, of which respondents accounted for 60, and withdrew 30 of the 84 introduced. Thus, the number of RTE cereal brands in the market increased from 26 in 1950 to 79 in 1973 [162] (Tr. 22,024, 22,029–31; CX 405). Broken down into five year periods, we find the following:

Initial Decision

99 F.T.C.

	<u>Brands Introduced Beyond Test Market</u>
1950-55	8
1956-60	15
1961-65	22
1966-70	19
1971-73	20

(CX 407)

582. Because of the influx of new brands, established brands lost market share. The top eight brands accounted for 47.3% of the market in 1964, a drop from 56.9% in 1954 (CX-PG 6B, C). Corn flakes, which accounted for 33% of total RTE cereal sales in 1940, had only a 10.8% share in 1972 (CX-K 7054A, 7148C, 7209D). From 1950 through April 1970, average market share per RTE cereal brand declined from about 4% to about 1.3%, and the average pounds sold per RTE cereal brand declined from around 22 to 18 million pounds. This was despite a substantial growth in total sales (Tr. 22,030-31; CX 409A).

583. RTE cereal pound sales increased by 78% between 1955 and 1972. Products introduced prior to 1955 accounted for only slightly more than 10% of this increase, while products introduced after 1954 accounted for almost 90%. By 1971, about 36.9% of RTE cereal sales consisted of products introduced in the prior 16 years (GMX 564). Respondents' products that existed beyond test market distribution prior to 1955 increased in aggregate pound sales by 107,125,000 from 1955 through 1970 (GMX 564E-F, I).

584. The parties differed in the degree of product introduction activity during the period. Whereas Kellogg was introducing products throughout the 1950's, General Mills increased its introductions in the mid-1950's, and both General Foods and Quaker increased their introductions in the late 1950's or early 1960's. After General Foods introduced Krinkles and Corn-Fetti in 1950 and 1951, it introduced only one more new RTE cereal product before 1959 (GFX 1370H).

585. Between 1950 and April 1972, Kellogg introduced 24 brands into test market or beyond (CX-K 1067); General Mills introduced 34 (CX-GM 2049, 2111); and General Foods introduced 21 (CX-GF 556, 18690).

586. Following General Foods' decision to emphasize its new product activities in FY 1962 (CX-GF 4039Z-17), it introduced nine [163]new RTE cereal products in the next five years (GFX 1370H-I). Quaker did not introduce a new RTE cereal product until 1961.

Kellogg introduced products at a fairly constant level throughout the complaint period, with slightly more activity in 1959 (CX 409B, E).

587. The respondents' success with new products differed. During the complaint period, Kellogg introduced nationally 16 new RTE cereal products. All but three found widespread consumer acceptance and were still on the market at the close of that period (Tr. 29,600-01; CX-K 1067, 7173; CX 434). The other respondents and Quaker all had varied success, with General Foods being the least successful (Tr. 27,009, 27,434, 38,331-32; CX-GF 4039Z-4). General Foods marketed fewer brands of RTE cereal in 1973 (15) than it did in 1964 (17) (GFX 1370).

588. The firms have also had differing success with respect to their already established products. Kellogg's older products have had a good deal of durability. Their sales increased by about 25% since 1958. Sales of General Mills' older products were flat; General Foods' sales of older products declined; and Quaker's sales of older products declined to a little more than half of their 1958 levels (Tr. 38,335-36; GMX 565).

589. Based on market share, the cereal industry became a business of relatively small brands (CX-GF 17A, D, 601Z-5, 602B; CX-K 7342C; CX-GM 2178D). An analysis of the peak market shares achieved by RTE cereal brands introduced from 1950 through 1972 shows that only seven of the 84 introductions had market shares exceeding 2% (CX 434):

BRANDS	YEAR OF INTRO.	PEAK SHARE AND YEAR
Kellogg's Sugar Frosted Flakes	1953	6.3% 1971
Kellogg's Special K	1956	4.1% 1970 & 1971
GF's Alpha Bits	1957	2.7% 1959
GM's Total	1961	2.6% 1967
Quaker's Cap'n Crunch	1965	2.4% 1965
Quaker's Life	1961	2.0% 1966 through 69
GM's Jets	1954	2.1% 1955

Of those seven, only Sugar Frosted Flakes, launched in 1953, achieved a 5% market share or better; only one achieved 4% or better; and the remaining five achieved between 2% and 3% at their peaks. No brand introduced after 1956 and before 1972 achieved 3% or more of the market. Respondents generally considered a new brand a success if it could sustain a market share in the 1% to 1.5% range (Tr. 11,723-26, 15,964, 17,746; CX 434J; CX-GM 2A, 179E, 276A, 591F, 603B, 700B, 2198B; CX-GF 20A-C, 30A, B, 470H, I, K, 1372F, H, 1389E, 2018A, C; CX-K 742A, 995). [164]

590. However, as indicated above, not all new product attempts

were successful. For example, from 1968 through 1971, six new products were introduced in the presweet segment of the RTE cereal market. Of these, at least five were definite failures (CX-GF 4010I, Z-39, Z-40).

591. As Quaker analyzed the 1958-1969 period (CX-Q 177H):

Since 1958, 76 brands of RTE cereal have been introduced into either test market or national distribution. Of these, only 54% are still on the market. Of the 36 RTE cereal brands on the market before 1958, 34 are still on the market.

The failure rate for new brands is even higher than indicated by these data since a considerable number of brands still on the market do not have a large enough share to qualify them as real successes. By dividing the study period into halves it appears that the number of introductions and the proportion of failures increased in the more recent years.

592. From 10 failures of 25 introductions in the 1958-1963 period, the failure rate increased to 35 of 51 introductions in the 1964-1969 period (CX-Q 177M). Altogether, 50% of the RTE cereal brands introduced beyond test market between 1950 and 1972 failed (Tr. 26,406, 26,416-17, 26,758-59; CX-GF 4010I, Z-39, Z-40; CX-Q 177H, M; CX-K 547B; CX 435).

593. Of 26 brands introduced prior to 1950 that were in the market in 1950, 23 were still available at the end of 1972. Of nine brands introduced in the five year period 1950-1955, eight were still available at the end of 1972. Comparable figures for subsequent five year periods are: 1956-1960, 10 of 21 still available; 1961-1965, 12 of 37 still available; 1966-1970, 15 of 42 still available (CX 435). These figures which show the number of brands that were withdrawn after introduction, do not reflect the numerous and costly efforts which did not culminate in products worth introducing, e.g., the cavity preventive RTE cereal effort of General Foods (*supra*, Finding 511).

594. General Foods, in particular, experienced difficulty during the 1960's in its introduction of new brands of cereal and was repeatedly unsuccessful (GFX 1370). It had costly failures in its attempts to develop and introduce cereals with freeze-dried fruits (Tr. 37,046-47).

595. The fixed costs necessary to launch a new individual brand include those of research and development of the brand, market research, production equipment and plant and introductory advertising (Tr. 21,964-65, 21,969-70). [165]

596. The fixed costs are significant. The major RTE cereal producers spend on average about \$180,000 to research and develop

and test consumer acceptance of each brand they launch (Tr. 21,969, 26,408; CX-CI 103Z-47; GFX 1153Z-47; CX-NC 500 at p. 34).⁵⁰ The major RTE cereal producers also spend substantial amounts for new plant and production equipment for many of their new brands (Tr. 21,970). Kellogg spent some \$4 million to \$6 million for new equipment for Product 19 (Tr. 13,203). General Mills planned expenditures of \$1.1 million and \$1.8 million, respectively, on new equipment for a new health and a new puff cereal (CX-GM 607E). The Danville plant of Quaker, used initially for King Vitamin, cost more than \$6 million.

597. The most significant fixed cost of launching a new RTE cereal is introductory advertising (Tr. 21,969-70).⁵¹ Newly introduced brands require disproportionately heavy advertising to achieve market penetration (Tr. 12,809; see CX 508A).

598. Substantial introductory advertising expenditures are necessary in order to persuade enough consumers to try new brands (Tr. 12,466-69, 14,435-39, 15,038, 15,771, 15,777-80, 17,301-03; CX-GF 4010Z-42, 4039Z-56; CX-GM 2180C). Unless it intensively advertises a new brand, an RTE cereal producer cannot get many retailers to place the new brand on their shelves. Retailers will not place a new RTE cereal brand on their shelves unless the manufacturer provides or promises to provide sufficient introductory advertising to "pre-sell" the new brand to consumers (Tr. 8919, 9185, 9348-50, 12,722-24). The high advertising level of the many RTE cereal brands already in the market (the high "noise level") requires high introductory advertising expenditures for new RTE cereals (Tr. 13,097, 14,437-38, 15,038, 15,243-44; CX-GM 557H). Kellogg's Marketing Director has stated:

It is not unusual for a new product introduction to involve an *initial* outlay for advertising and promotion money that far exceeds the total dollar volume of sales for the first year's introduction. Unless the product succeeds in an *unusual* way—it may become virtually impossible to *ever* recover [166]the cost of introducing the new product (CX-K 552G) (emphasis in original).

599. By late 1961 or early 1962, General Foods concluded that introductory advertising expenditures of around \$3.5 million were necessary to launch a new brand expected to achieve a 1% market share (CX-GF 17A, D). General Mills stated that the heavy introductory advertising it planned for Smiles (\$4.1 million) was essential for success (CX-GM 603E, H, W). The respondents and Quaker spend

⁵⁰ General Foods spent between \$150,000 and \$300,000 on research and development for Alpha Bits during its first three years (Tr. 13,436, 13,635-37).

⁵¹ Advertising during the first 12 months a product is placed in national distribution is considered introductory advertising.

substantial sums on introductory advertising for each brand they introduce. Between 1956 and 1972, they spent on average some \$3.2 million per new brand (Tr. 26,399-404; CX 206, 508; CX-Q 177Z-20).

600. Not only are the fixed costs of developing and introducing a new product very high, but there is an extended leadtime in going from the drawing board to national distribution and in reaching a break-even point. Dr. Schmalensee, complaint counsel's economic expert, agreed that it takes approximately four years to get a new product off the drawing board and into national distribution and another three years to achieve a break-even point on the product (Tr. 23,413-14).

601. General Mills' development time for Mr. Wonderful's Surprise and Golden Grahams, products that required new technology, was in excess of 10 years (Tr. 32,990). For products developed primarily on existing technology, General Mills' development time averaged from five to six years (Tr. 17,237, 32,989). General Mills began experimental work on Buc Wheats in 1964, but did not introduce the product Buc Wheats until 1971 (Tr. 32,914, 32,989).

602. The foregoing demonstrates that respondents engaged very heavily in new product competition; that this method of competition was expensive and risky and that there was a long period of time before even a successful new product venture would pay off. It has also been demonstrated that, as a result of respondents' new product competition, individual cereal brands on average accounted for smaller shares of the market and lower poundage of sales.

V. IMPEDIMENTS TO NEW ENTRY INTO THE RTE CEREAL INDUSTRY

A. Brand Proliferation

1. Complaint Counsel's Theory

Complaint counsel (CPF 9-1 thru 9-338; CRPF 9-1 thru 9-112) would place responsibility upon respondents for the lack of new entry into [167]the RTE cereal industry. The following is a summary of complaint counsel's theory of the existence of a barrier to entry and respondents' responsibility therefor.

The RTE cereal industry has enjoyed supracompetitive profits (an issue which will be dealt with later in this initial decision) and was growing rapidly. This should have attracted new entry into the industry. The absence of such entry indicates the existence of a barrier to entry. Respondents' brand proliferation conduct raised effective barriers to the entry of new RTE cereal producers and provides the complete answer to this absence of entry. While brand

proliferation is not in itself unlawful, respondents must be held responsible for its deterrent effects upon entry, since respondents turned to this method of competition as a result of their mutual avoidance of other means of competition.

As I have already found (*supra*, Findings 529-31), brand proliferation in this case is nothing more than the introduction of new brands as a legitimate means of competition and did not result from any other activities of respondents. Thus, respondents cannot be held legally responsible for the impact upon potential new entrants of their introduction of new products. However, for purposes of providing complete findings, I shall continue with complaint counsel's theory of respondents' brand proliferation as the sole barrier to entry into the RTE cereal industry.

The proliferation is said to be of highly-differentiated, intensively advertised, trademarked, new RTE cereal brands. The brands actually differed to varying degrees or, by reason of advertising, the consuming public was led to believe they differed. In this manner, competition among RTE cereal brands was "localized"—the first of three basic conditions under which brand proliferation will cause a barrier to entry.

When competition is not localized, a change in price, advertising or promotion of one brand would equally affect all other brands, and industry-wide reaction could be anticipated. The introduction of a new brand would similarly affect all other brands in the industry. A potential entrant would look to the market as a whole for its source of sales and would anticipate being able to take comparable percentages of sales from all existing brands. Any reaction to the new entry by existing competitors would impact all brands in the market.

On the other hand, when competition is localized, a change in price, advertising or promotion of one brand would affect primarily the other products in the segment in which it is located, and reaction would be anticipated only from the other brands in the segment. The introduction of a new brand would affect significantly only the brands in the segment into which the new brand had been introduced. The potential entrant could look only to the segment [168] into which it was considering entry for its source of sales. Existing competitors would react only in the segment involved without impacting other brands in the industry. In sum, the new entrant would have a more limited area from which it might secure sales and it would anticipate more direct competitive reaction from the existing brands in the segment it had entered.

The second basic condition, under which complaint counsel assert

that respondents' brand proliferation has created a barrier to entry, is termed "brand immobility." This means that the attributes of existing brands are so firmly established in the minds of consumers that the brands cannot be repositioned to appeal to those who want different attributes. Consequently, when a new brand is entered into a segment, existing brands cannot avoid competition by changing their appeal but must meet the competition of the new brand head on. A potential entrant, therefore, would anticipate this head-on competition from existing brands in the segment considered for entry and so might be deterred from entry.

The third basic condition of complaint counsel's assertion that respondents' brand proliferation has created a barrier to entry is the existence of substantial fixed costs associated with the development and introduction of a new product. These are production, marketing and distribution costs which do not vary directly in proportion with the amount of the item produced.

Respondents are said to have so crowded the market with their products that the introduction of additional, profitable brands by new entrants has been foreclosed.

As the demand for cereals grew, opportunities for new brands did occur. Except for the granola or natural segment of the market, these opportunities or "holes" in the market were filled by the six existing major producers. This is because the existing majors were already operating at an overall efficient scale, so that it was profitable to add an additional product even though the volume of that product alone would not cost justify an outsider entering the RTE cereal industry. An outsider would need several simultaneous successful product entries of the size that can be anticipated in this industry before it could operate at minimum efficient scale and so not be at a cost disadvantage to respondents.

This would be most unlikely since it is difficult to develop successful brands; and by the time an outsider could be ready with several brands, an existing firm could fill any particular hole or opportunity that might exist.

In sum, complaint counsel assert that there is a product efficiency of scale equal to about 1% of the market, whereas firm efficiency of scale is not reached until sales of 3.5% to 5% of the market are achieved. Respondents, all of whom are already operating [169]at or above firm efficiency of scale, can introduce a new product whenever a 1% opportunity appears, whereas an outsider cannot. The outsider is faced with the insurmountable task of finding simultaneously three or more opportunities in order to enter the market at

minimum firm economy of scale so as not to be at a cost disadvantage to respondents.

Complaint counsel assert that an outsider would have to find larger individual holes or opportunities than respondents since respondents do not react to each other in a competitive fashion, whereas they would react very strongly to an outsider's entrance in a particular, limited segment.

The requirement to achieve entry by multiple brands is also said to have deterred entry since the entrant would have to expend large capital costs on each of the several brands to be introduced. Complaint counsel assert (CP 9-29):

The conclusion that respondents' brand proliferation practices have increased a potential entrant's capital costs is based on the previous analysis demonstrating that a potential entrant can no longer expect to attain entry at efficient operating scale with a single brand. The necessity of a multi-brand strategy means that the entrant must fund several research and development efforts, several introductory advertising programs, and possibly several production lines. The record shows that it is much more expensive to develop and introduce five brands whose total sales will fall in the range of from 3.5% to 5% of the market, than it is to develop and introduce a single brand to achieve the same market share. The additional costs of entry via a multi-brand strategy are so great that many smaller firms simply cannot raise the necessary capital. The magnitude of the required capital does not prevent entry by the largest firms, but it does result in their acting more cautiously. If the cost of entry were significantly lower, the attractiveness of the industry would result in more frequent gambles by many firms. But as the costs grow, fewer gambles are taken and firms are likely to exercise such great caution that by the time they have decided to enter, their original brand ideas may have been preempted by one or more brand introductions by respondents. [170]

2. Localization⁵²

603. Localization or segmentation of brands is the first of the three necessary conditions under which, according to complaint counsel, brand proliferation will cause a barrier to entry. As I have previously found (Findings 59-150), there are segments or categories of cereals within which brands compete more strongly with each other than with other brands because of their similar attributes, and there are some cereals that are so similar that they compete with each other on a one-to-one basis. The record, however, does not permit an exact delineation of the segments and the degrees to

⁵² Consumers' desires for variety in breakfast are responsible in large measure for the differentiation of RTE cereals (*supra*, Finding 532). Respondents, for example, may be said to have reacted to children's desires for presweetened and flavored cereals, to many consumers' desires for natural cereals and to many other consumers' desires for fortified cereals. Respondents, therefore, may not be held responsible for localization of this nature. Localization, to the extent it has come about by what complaint counsel term "brand proliferation" is the result of competition by means of introducing new products to appeal to the varying desires of different categories of consumers.

which competition among cereals is confined to those cereals in particular segments. The necessary corollary to this description of localization, as shown to exist in the RTE cereal industry, is that some cereals have a broader appeal than the particular segment or category in which they fall so that they compete to varying degrees with cereals outside of their category.

604. For example, adult products, such as Total, Special K, Product 19, All Bran, 100% Bran and 40% Bran Flakes, not only compete with each other, but also compete strongly with all-family products, such as Cheerios, Rice Krispies, and Corn Flakes. And children's products, which are essentially the presweets, not only compete with each other but compete strongly with the all-family products (Tr. 35,367-70; GMX 194, 195, 546A, 547A-B, 548A-B, 549A). While some presweets compete more directly against other presweets, all 30 or so presweets compete to some degree with each other (CPF 9-172; CX-GF 4K, 1410A, 1439, 3000Z-95; Tr. 22,778-81). Grape Nuts competes with all RTE cereals for its share (CX-GF 40), while Post Raisin Bran competes strongly with General Foods' presweetened cereals (GFX 1210Z-5).

605. Twenty-one other brands each accounted for over 1% of the RTE cereal consumption of the two-member families that purchased [171]Cheerios in 1969-1970. For 1975-1976, 25 other brands each accounted for more than 1% of their consumption (GMX 518A-B). Two-member families consuming Kellogg's Corn Flakes had more than 1% of their consumption accounted for by each of 20 other brands in 1969-1970 and by each of 23 other brands in 1975-1976 (GMX 520A-B).

606. Many consumers of RTE cereals are interested in many product attributes such as puffing, flaking, specific grains, shapes, textures, flavors and degrees of sweetness. The number of directly competing brands is determined by the number of attributes relevant to each consumer's purchasing decisions. The number of direct brand competitors increases as the number of attributes relevant to particular consumers increases (CPF 9-185, 9-186, 9-188; Tr. 21,953-54, 22,078-80, 22,771-78, 26,253-54).

607. It is uncontested that RTE cereal products compete on the basis of varying numbers of in-common characteristics that differ in importance, but that no analysis was made to quantify the numbers of direct competitors as a result of these in-common characteristics (Tr. 22,753-54, 22,777, 22,794, 23,892-93).

Inasmuch as localization is a necessary predicate to complaint counsel's barrier to entry by proliferation theory, the question arises whether localization exists to the degree required. As an abstract

theory, it is logical to assume that a new product's success would be limited by the size of the area or segment within which it is to compete. However, to the extent that it may draw customers from outside of its primary segment, its success potential becomes less limited.

608. While the extent to which localization prevails in the RTE cereal industry is an unknown, it exists to a sufficient degree to have the type of impact theorized by complaint counsel.⁵³ Respondents believed that the effect of increasing the number of brands on the market was to increase segmentation (CX-GF 17A, D), fractionalization (CX-K 7342C; CX-GM 2178D), or fragmentation (CX-GM 601Z-5). "The cereal industry has become a business of small brands." Kellogg believed that "a lot of products on the market in 1970 will account for *less than one percent*," as a result of the continued introduction of new brands. This would result in fewer brands with large market shares (*i.e.*, 3-5%) (emphasis in original) (CX-K 565J). [172]

3. Brand Immobility

609. Brand immobility is the second of the three conditions under which complaint counsel contend that respondents' brand proliferation has caused a barrier to entry. While I would not expect that a manufacturer of an existing product would, even if it could, reposition a product to accommodate a new entrant,⁵⁴ the condition of brand immobility has been established on the record.

610. It is difficult to reposition a product from an idea or concept that people have gained. It may be hard to get people to accept the product's new position if they have associated the product over time in its former position. There is a good deal of risk and expense involved in trying to change people's established concept of a product (Tr. 14,212-13, 14,466-68). General Mills has learned that when you try to make radical changes, you sometimes lose the entire market. It doesn't make sense to reposition an RTE cereal product after it has gone national (Tr. 15,762-63, 17,707-11; CX-GM 2476F-H).

611. Attempts at repositioning have failed. Kix was originally an all-family cereal. It had always had some consumption by children. As Kix's sales declined, General Mills attempted to move the brand more toward children. General Mills changed the package, used

⁵³ Since localization is an element in evaluating crowding, the comments at the end of my findings on crowding (*infra*, Finding 621) apply equally here.

⁵⁴ With the large number of products in the market catering to all nature of consumer wants, there would be no point to the manufacturer of a successful existing product to pick up and run from a new entrant and attempt to compete in a different area. There is no evidence that an existing brand has ever been repositioned to accommodate a new brand.

