

# Economic effects of online marketplace bans

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## Key findings and implications

### **SMEs leverage online marketplaces to grow their retail business in the digital world**

SMEs make up **52 percent** of EU retail – one of the most important sectors to the EU economy. With more and more consumers moving online and shopping 'multi-channel', retailers are flocking to have an online presence.

Today, **46 percent of SME retailers** leverage online marketplaces that help them to establish and grow a multi-channel presence comparable to that of large firms. SMEs find this sales channel a particularly convenient model. Using online marketplaces, SMEs sell online at lower IT cost than needed for running an own website shop while gaining a consumers' reach (domestic and cross-border) that an own website shop would find hard to achieve. The existence of this successful model, with a strong potential yet to be harnessed, is great news for SMEs and for the European Digital Single Market.

### **Online marketplace bans are on the rise**

Manufacturers, brands, and other suppliers have reacted to the increased online commerce competition by putting in place distribution restrictions. Online marketplace bans are today a **widespread** and rising practice that affects e-tailers of all sizes, in many EU countries and across many product categories to a similar, strong extent. These bans, imposed by suppliers in their distribution contracts, stop SME e-tailers using online marketplaces to sell products of the brand imposing the ban. They thereby disable a retail sales channel that has become important for both SME e-tailers and consumers.

### **Online marketplace bans create potential losses of 53 percent of SME e-tailers' total online revenue**

Online marketplace bans harm many small e-tailers in many ways. The most immediate effect of online marketplace bans lies in a decrease sales revenue for e-tailers selling on online marketplaces. SME e-tailers indicate that they stand to lose **53 percent** of their total online revenue from pervasive online marketplace bans. This is supported by analysis of e-tailers' sales revenue on the eBay online marketplace. Beyond this, SME e-tailers' long-term customer relations and profitability are put at risk when online marketplace bans are imposed.

Moreover, pervasive online marketplace bans undermine the key benefits that online marketplaces present to SME e-tailers, such as starting up and getting online as well as benefiting from the boom in m-commerce. Online marketplace bans are likely to counteract the cross-border sales development that SME e-tailers have achieved thanks to online marketplaces. Consequently, such bans impair the EU policy aim of a frictionless, ever more deeply integrated Digital Single Market – particularly for SMEs.

### **Online marketplace bans harm consumers**

Online marketplace bans impact consumer welfare by taking away the convenience-enhancing features that online marketplaces present to consumers concerning the easy of search, transparency and time efficiency of the purchase.

### **Online marketplace bans may harm competition**

Online marketplace bans lead to a restriction of competition between retailers of the same brand (intra-brand competition) that may not be sufficiently outweighed by competition between brands (inter-brand competition) nor by the unsupported efficiency gains arising from these bans.

### **€ 26 billion at risk for SME e-tailers**

Unless EU institutions send a clear signal that online marketplace bans are not permissible, this would likely lead to an increased use and enforcement of these bans by brand owners. As a result, in a scenario where online marketplace bans become pervasive, this would result in a strong impediment to SME e-tailers. This would cause a major upheaval in retail commerce, depriving e-tailers of an estimated **€26 billion** of online retail sales, diverted elsewhere.

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## Executive summary

The retail sector is a fundamental component of the EU economy. At its heart is a large variety of micro, **small and medium enterprises (SMEs)** which compete to serve the evolving needs of European consumers and make up **52 percent** of EU retail. This sector's mission is to be where consumers' lives take them and to provide the goods that consumers demand.

Consumers are nowadays shopping in a multitude of ways and use a variety of different channels. Online shopping now complements shopping in traditional brick and mortar stores. Busy consumers use their smartphone to make the most of their time available (e.g., on public transport or other idle time) to search for product information and prepare or to shop. Unsurprisingly, retailers are flocking to have an online presence (and thus become e-tailers), since this is how consumers now spend an increasing share of their time.

To establish and grow this online presence a large share of SME retailers leverage online marketplaces – websites and mobile apps that allow independent retailers to transact with consumers via the online marketplace platform. SMEs find this sales channel particularly convenient as it allows them to sell online with a fraction of the IT costs that would otherwise be needed to set up and run an own website shop – while attaining a consumer reach (domestic and cross-border) that an own website shop would find it hard to achieve.

**Figure 1 Symbiosis between online marketplaces and e-tailers**

	<p><b>LOWER COST</b> Less costly way to set up and run an online business</p>	 For <b>68%</b> of German retailers set-up costs are a fairly/ very important reason to not sell via an own website shop
	<p><b>WIDER REACH</b> More traffic than on own website shop</p>	 <b>85%</b> of German retailers see lack of traffic as biggest hurdle for selling online via an own website shop
	<p><b>MOBILE REVOLUTION</b> Only online marketplaces enable SME e-tailers to take part fully and efficiently</p>	 Consumers will use a limited number of shopping apps from big providers Online marketplaces are currently the most popular shopping apps
	<p><b>NEW TECHNOLOGIES</b> Online marketplaces offer SMEs access to new, disruptive technology</p>	 Personalised shopping assistants via social media (e.g., eBay's ShopBot) Artificial intelligence to improve shopping experience (e.g., Etsy's Blackbird)

Source: Copenhagen Economics compilation of multiple sources computed in the main body of the text.

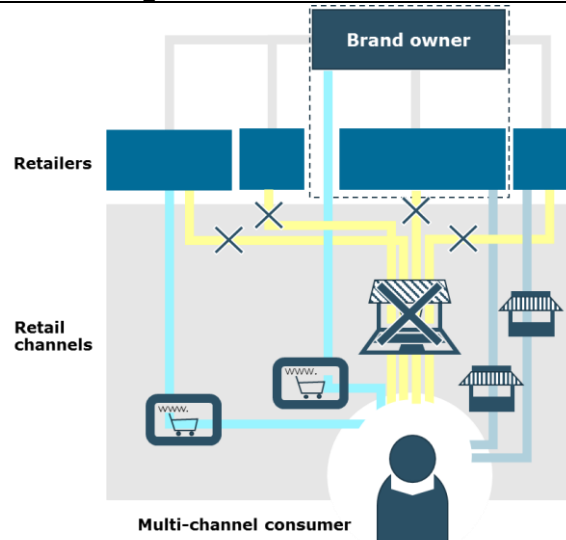
Retailers (including for their online activity) depend on players that are upstream in the value chain and supply products to them on a wholesale basis – with many of these products being branded goods. However, a fast-increasing number of large brand owners have started to impose contractual restrictions, called online marketplace bans (OMBs) as part

of their selective distribution policies. These bans prevent SME e-tailers' from leveraging online marketplaces to sell products of the brand imposing the ban.

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**Figure 2 Online marketplace bans**

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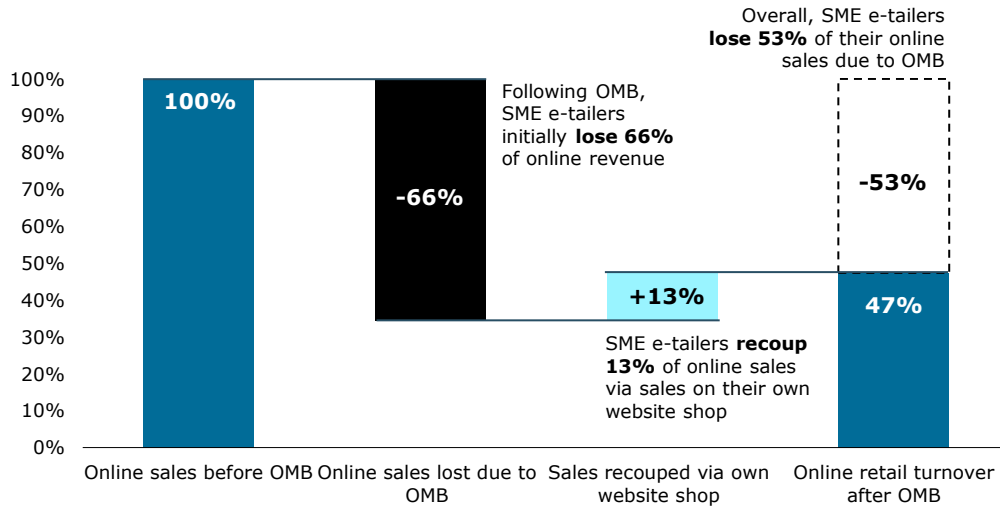


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Source: Copenhagen Economics.

In theory, e-tailers may be able to avoid being affected by such a ban by adjusting the way they do business, for instance by choosing to stock other brands or to focus more on traditional brick and mortar sales, which are never targeted by brand owners' bans, or invest effort to setup and market an own website store.

However, in practice, this is not a viable option for SME e-tailers, as they leverage online marketplaces to reach out to consumers, which are their vital source of income. When surveyed, SME e-tailers report that online marketplace bans affect not just their online sales but also their overall turnover.

**Figure 3 SME e-tailers' sales loss from pervasive OMBs**

Note: Additional analysis (other retailer size categories; recoupment analysis) is presented in the Appendix to this report.

Source: Copenhagen Economics based on Morar (2016) e-tailer survey.

### Online marketplace bans, unless halted, would have a major impact on retail

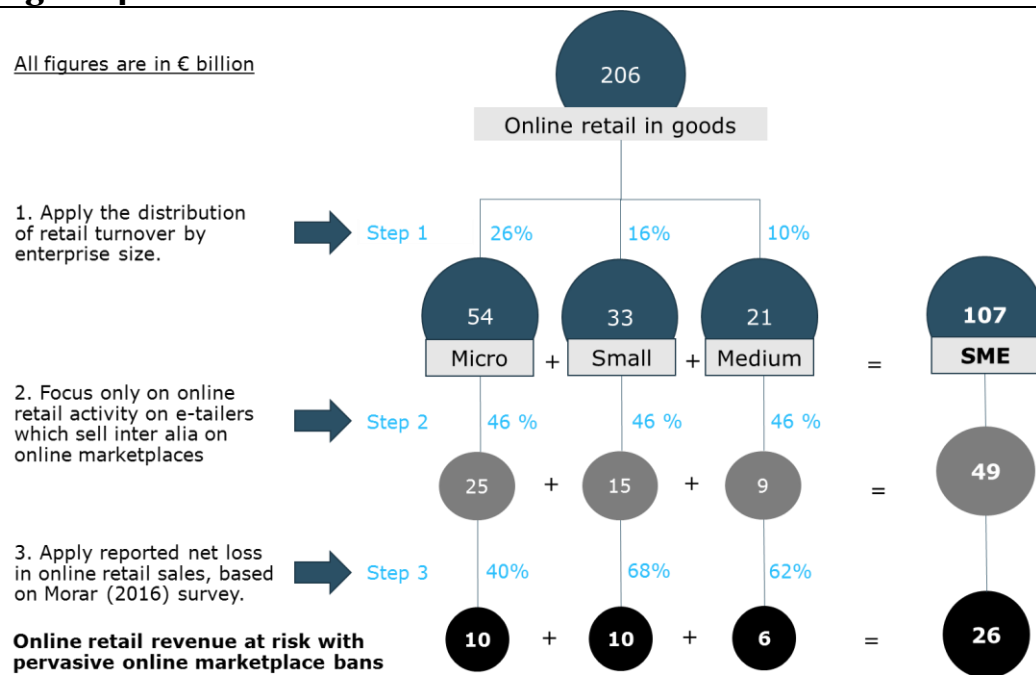
Online marketplace bans are currently in a competition law grey area. In the past, different types of bans imposed by brand owners (online bans) were also in a grey area, until the Court of Justice of the European Union found them to be incompatible with EU competition law (see the Pierre Fabre case<sup>1</sup>), which resolved the uncertainty for blanket online bans. However the legal uncertainty persists today for online marketplace bans, which allows brand owners to experiment with online marketplace bans.

Moreover, the European Commission has launched an inquiry into the functioning of the e-commerce sector, which has identified online marketplace bans as a key restriction.

Unless EU institutions send a clear signal that online marketplace bans are not permissible, this would likely lead to an increased use and enforcement of these bans by brand owners. As a result, in a scenario where online marketplace bans become pervasive, this would mean a strong impediment to SME e-tailers. This would cause a major upheaval in retail commerce, depriving e-tailers of an estimated €26bn of online retail sales, diverted elsewhere.

<sup>1</sup> C-439/09 – Pierre Fabre Dermo-Cosmétique, 13 October 2011.

**Figure 4 Online retail revenue at risk due to OM ban**



Note: Step 1 is based on Eurostat (distribution of retail enterprises, by turnover); Step 2 is based on Eurobarometer 439, p. 12; Step 3 is based on Morar (2016) e-tailer survey, Question 9 "If all brands imposed platform bans how much business would you lose in sales/revenue?", Question 10 "In the same situation with platform bans for all brands, what share of the sales/revenue lost would you be able to recoup by selling brands via other channels (e.g., your own website or brick and mortar retail)?".

Source: Copenhagen Economics estimates based on EC JRC (Duch-Brown and Martens, 2015), Eurobarometer (2016), Eurostat (2016), Morar (2016) e-tailer survey.

**The European Digital Single Market at a crossroads**

The SMEs’ model to leverage online marketplaces for establishing and growing a multi-channel presence comparable to that of large firms is a successful model with strong potential yet to be tapped into. This is in particular because of the reduced barriers to cross-border retail trade for SMEs when they leverage online marketplaces. The existence of this model, now well proven and established, is great news for the European Digital Single Market.

Moreover, by restricting SME e-tailers’ ability to reach consumers on the online channels where consumers preferences are increasingly evolving to (e.g. mobile commerce, app-based e-commerce), these bans are likely to harm consumers by forcing a sub-optimal retail experience, compared to the consumers’ desired retail channel and brand preferences.

In conclusion, the legal grey area surrounding online marketplace bans seems at odds with the flagship EU policy of achieving a fuller, deeper Digital Single Market. EU policy-makers strive to promote the digital transformation of the European economy. It appears highly inconsistent with these policy objectives that one of the top EU sectors of economic activity – the retail sector – is discouraged from going online in an efficient way, due to the effect of online marketplace bans.

## Chapter 1

# SMEs serve retail consumers better via online marketplaces

SMEs, which are the backbone of the EU retail and online retail sector, strongly use online marketplaces to sell online and, in particular, to sell *cross-border*.

The importance of online marketplaces for SMEs is grounded in their symbiosis with online marketplaces. Online marketplaces support SMEs in getting online, growing online, being competitive online in terms of cost, reach and digital innovation, to overcoming the frictions of the internal market and selling cross-border.

Moreover, online marketplaces benefit consumers in a way that other sales channels (e.g., shopping on online website shops or in brick and mortar stores) cannot.

This chapter analyses how the provision of retail services benefits from the activity of online marketplaces. As a result, this is advantageous both for the suppliers of retail services (the vast majority of which are SMEs<sup>2</sup>) and for its recipients, i.e. all of us as retail consumers.

### 1.1 Digital transformation in the retail sector

The retail sector's *raison d'être* is to be where consumers' lives take them and to provide the goods that consumers demand in the most convenient way. If a large number of consumers were to move to the moon, we would see retail outposts on the moon. If all of consumers' free time were to be spent exercising in parks, we would see the retail industry reorganising itself to find further ways to follow consumers' exercise habits.

Today, consumers are not going to the Moon but, more mundanely, they are moving a greater share of their lives online. This is because consumers enjoy the convenience of the information and possibilities offered by the internet and internet-enabled devices such as smartphones and tablets.

As a result, consumers are nowadays shopping in a multitude of ways and on a variety of different channels. Shopping in the traditional brick and mortar stores is now complemented with online shopping. Busy consumers use their smartphones to search for information and make the most of their time available (e.g. on public transport or other idle time) to prepare and to shop.

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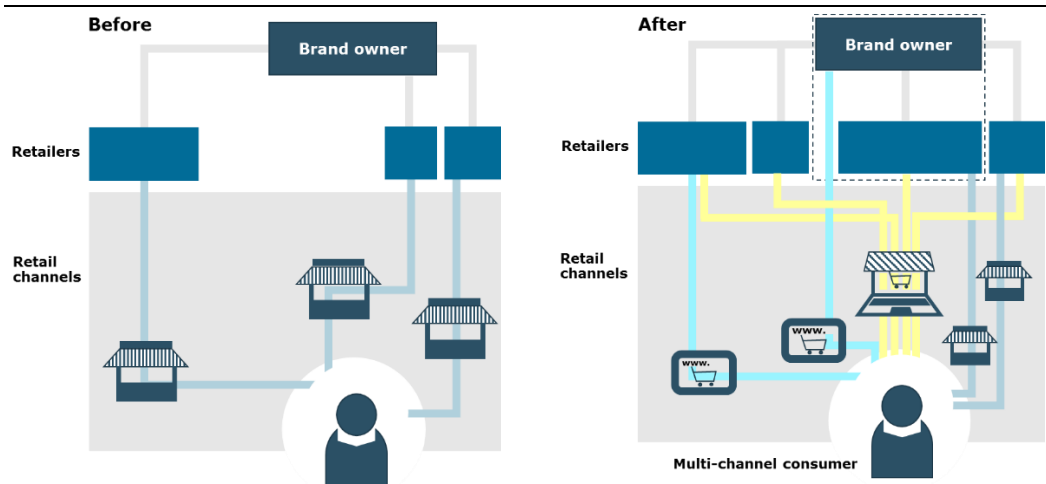
<sup>2</sup> We define SMEs as including micro enterprises (< 10 employees, ≤€ 2 million annual turnover), small enterprises (< 50 and ≥10 employees, >€ 2 million and ≤ € 10 million annual turnover) and medium-sized enterprises enterprises (< 250 and employees, >€ 10 million and ≤ € 50 million annual turnover).

Therefore, retailers, including their rump of SMEs, are flocking to establish and develop their online presence, since this is how consumers now spend an increasing share of their time, and serve retail consumers' needs and evolving preferences, thus becoming SME e-tailers. Any retailer's competitiveness derives from a superior ability to offer a range of goods that consumers will want to buy (including branded goods), to offer them in the right way, in the right location, i.e. channel, and at the right price.

However, the vast majority of SME e-tailers are not companies with an IT background – they are companies with a retail background, with competences in product sourcing, demand monitoring, and customer service. Therefore, for SME retailers, which are not native in online skills, online retail means an opportunity as well as a challenge.

In order to establish and grow this online presence, a large share of SME retailers leverage online marketplaces – websites and mobile apps that allow independent retailers to transact with consumers via the online marketplace platform (the retail channel depicted in yellow in the figure below).

**Figure 5 Retail distribution of branded goods before and after the advent of the internet**



Source: Copenhagen Economics.

Just as is the case in the brick and mortar world, also online many consumers not only shop from large retail firms but appreciate as well the smaller retailers and enjoy the choice and the discovery process that a diverse retail environment offers them. Unsurprisingly, just as it is enjoyable to browse through a Christmas market, a farmers' market or a shopping mall, so do many consumers enjoy browsing through their digital equivalents: online marketplaces.

As the online retail channels becomes an increasingly central part in the interaction between retailers and consumers, this leads to three key implications.

First, for retail and wholesale firms the digital transformation brings opportunities and challenges to achieve greater efficiency. Digitisation changes not only retail customer needs but also the management skills needed by retailers, the business models possible (e.g. retail channels mix) and ultimately changes the skills requirements.

Second, e-commerce induces players at different steps in the retail value chain to compete more intensely:

- against players somewhere else (up/down) in the value chain, e.g., a specialised retailer competing with the brand owner's own (online) stores
- against players somewhere else geographically (cross-border trade i.e. in the EU Single Market)
- across channels (brick and mortar stores vs. online webstores vs. sales on online marketplaces)

Third, the above disruption in the retail sector and the more intense competition ultimately centres around a consumer that has never before been as empowered as today.

The “journey of a shopping purchase” is rife with possibilities for consumers today. Consumers enjoy multiple retail channel shopping experiences. Along every different type of retail channel, consumers gather information on products, choices, other consumers' experiences and prices before finalising each purchase in a potentially different way, according to convenience and to suit their preferences.

Ultimately, the retail sector will be in healthy shape if consumers remain centre-stage and can manage what retail channels they prefer to use, how to use them and when to use them – rather than have some players in the retail value chain trying to police the value chain and limit the choice and convenience available to consumers.

## **1.2 SMEs leverage online marketplaces to grow their retail business in the digital world**

### **SMEs are the backbone of the EU retail and online retail sector**

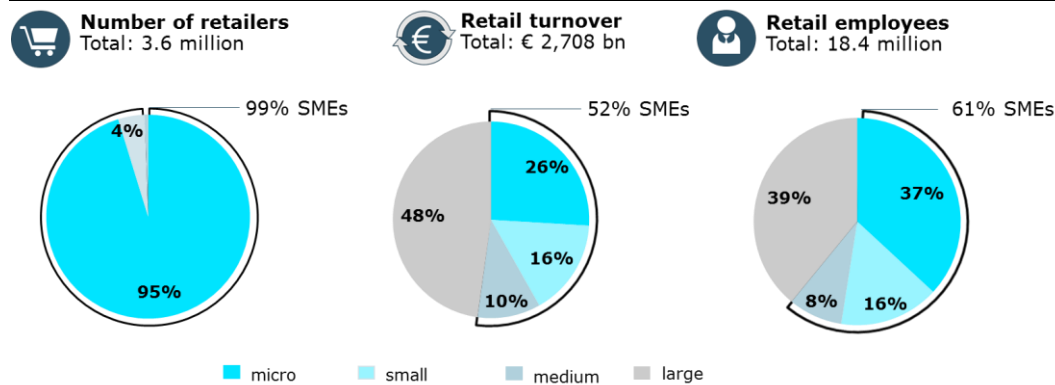
The retail sector plays a crucial role in the EU economy, accounting for 8 percent of EU total jobs and 15 percent of all EU private sector companies in 2013.<sup>3</sup>

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<sup>3</sup> Oxford Institute of Retail Management (2014).

SMEs are the backbone of the EU retail sector. In 2013, **99 percent** of all retailers in the EU were SMEs. In the same year, SMEs account for **52 percent** of EU retail turnover and **61 percent** of employment in the retail sector, see Figure 6.

**Figure 6 Role of SMEs in EU retail, 2013**



Source: Copenhagen Economics based on Eurostat.

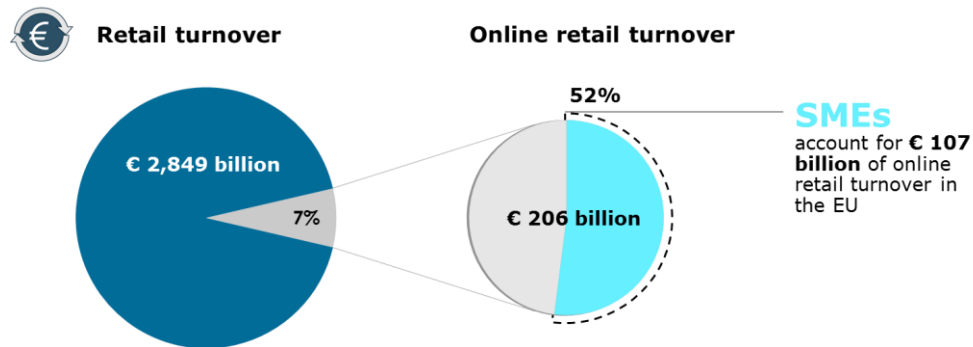
Today, an increasing share of retail sales take place online. In 2014, online retail accounted for 7 percent of total EU retail sales.<sup>4</sup>

SMEs follow consumers into the digital world, becoming SME e-tailers. SME e-tailers are at least equally as important for online retail as SMEs are for ‘traditional’ retail. We estimate that SME e-tailers account for about half of the revenue of the € 206 billion of economic activity in online retail. In other words, SME e-tailers’ contribution to online retail in the EU in 2014 amounted to € 107 billion, see Figure 7.

<sup>4</sup> EC JCR (Duch Brown and Martens 2015), p. 7.



**Figure 7 SME contribution to EU online retail, 2014**



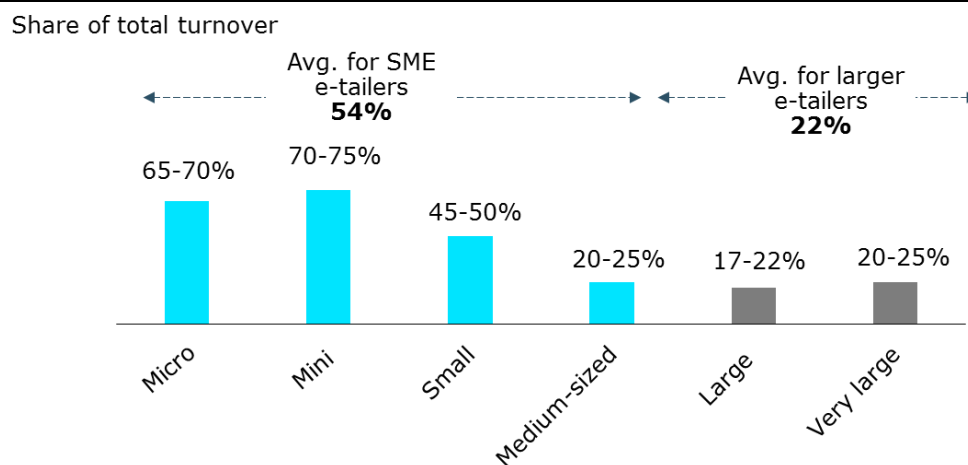
Note: While 2016 forecasts exist, 2014 is the latest year for which confirmed statistics are in place. We assume a 52% share of SMEs in total online turnover equal to the 2013 share of SMEs in overall retail activity (both brick&mortar and online) reported by Eurostat.

Source: Copenhagen Economics based on Eurostat and EC JCR (Duch Brown and Martens 2015), p. 7.

**SMEs leverage online marketplaces to a great extent**

When selling online, SME retailers extensively use online marketplaces. Across the EU, 46 percent of SME retailers use online marketplaces.<sup>5</sup> A recent EC consultation shows that SME retailers selling online both via online marketplaces and via their own website shop make 54 percent of their turnover from sales via online marketplaces, against only 22 percent for larger retailers, see Figure 8.

**Figure 8 Turnover from online marketplace sales by retailer size, 2015**



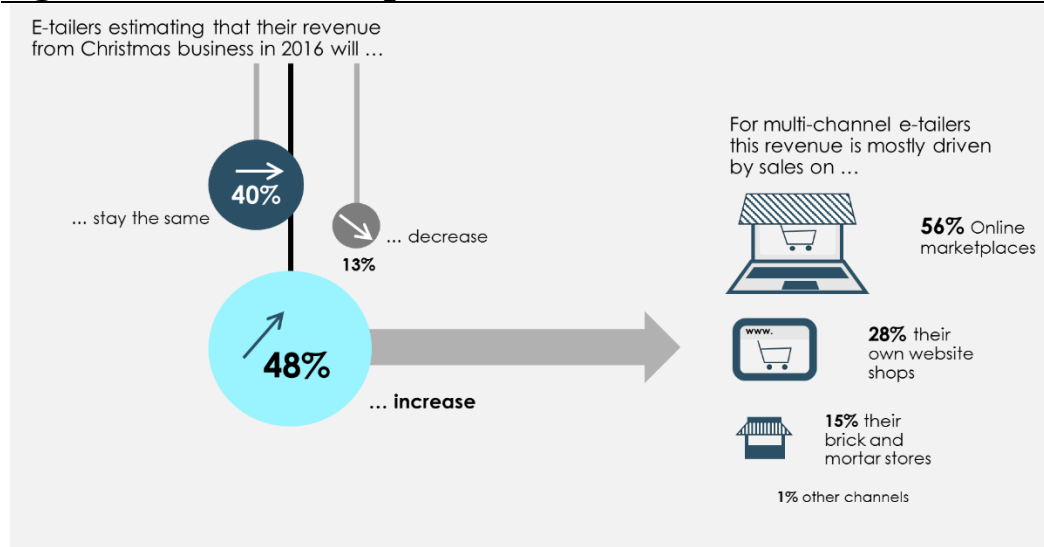
Note: This figure refers to retailers that sell both on online marketplace and via an own website; based on figures published by the European Commission and averaged via the distribution of turnover in the retail sector as measured by Eurostat (2013).

Source: Copenhagen Economics based on EC (2016 A), p. 119.

<sup>5</sup> EC (2016 A), p. 12; SME figure is composed using the distribution of micro, small and medium enterprises in EU retail turnover (Eurostat, 2013).

Another illustration of the importance of online marketplaces as sales drivers is their importance for multi-channel retailers' Christmas sales. According to an ECC survey, 56 percent of German multi-channel e-tailers estimate that their Christmas revenues will be mostly driven by sales via online marketplaces.

**Figure 9 Online marketplaces drive Christmas sales revenue**

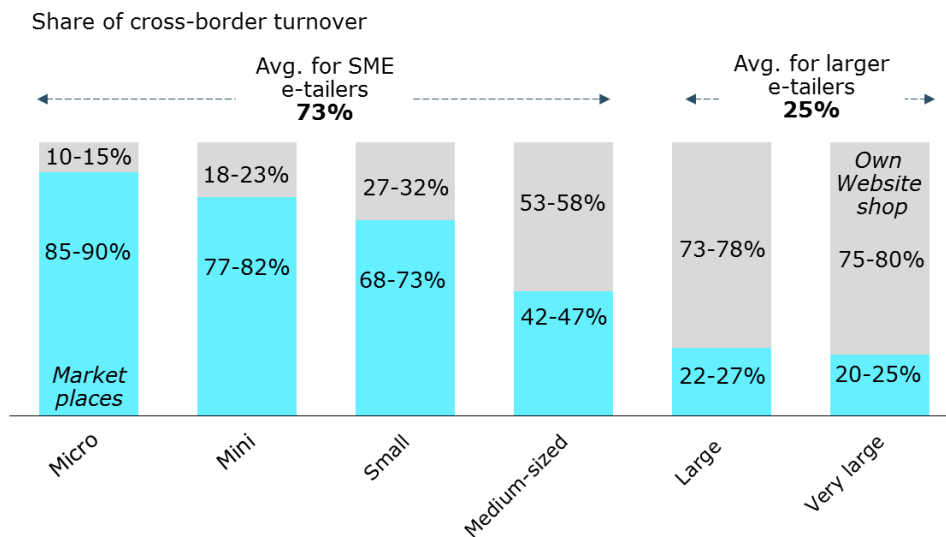


Note: Numbers are rounded.

Source: Copenhagen Economics based on ECC (2016) KIX Konjunkturumfrage unter Onlinemarktplatzhändlern.

Furthermore, SME e-tailers are even more reliant on online marketplaces when it comes to cross-border sales. A recent EC consultation finds: the smaller the retailer respondents, the more they leverage online marketplaces for cross-border online sales and the less they use their own website shop. On average, the SMEs surveyed leverage online marketplaces for 73 percent of their cross-border turnover, see Figure 10.

**Figure 10 Cross-border turnover from online marketplaces sales and sales via own website shop, by retailer size, 2015**



Note: This figure refers to retailers that sell both on online marketplace and via an own website; based on figures published by European Commission and averaged via the distribution of turnover in the retail sector as measured by Eurostat.

Source: Copenhagen Economics based on EC (2016 A), p. 119.

We analyse in a section below in greater detail the drivers for SMEs' use of online marketplaces to sell cross-border, identifying the set of benefits for SME e-tailers.

### 1.3 Symbiosis between SMEs and online marketplaces

Selling their products online provides many opportunities for SME retailers. Online, SMEs no longer face the physical limitations of physical shops and storage facilities. Technically, there is no limit to the number of products that they can offer online. At first sight, digitisation has also lowered entry barriers for SMEs. For instance, for an SME retailer that already offers its products for sale in a brick and mortar store, start-up cost to also provide its products online should be relatively low.<sup>6</sup>

However, just like in the offline world, SME e-tailers face similar challenges related to starting and growing their own business online while remaining competitive in terms of costs, consumer reach and while selling across the border to consumers in other countries.

In fact, some of the competitive disadvantages that SME retailers face compared to larger retailers in the offline world might reproduce themselves (in a similar or different manner) in the online world.

<sup>6</sup> Bundeskartellamt (2013).

This is where online marketplaces come into play: they provide smaller retailers with some of the advantages of the online world that would otherwise be reserved to larger retailers. It is in the online marketplaces' interest to do so, since having SMEs on board makes the marketplace more relevant to consumers and thus supports the marketplace's business.

Equally, the importance of online marketplaces for SMEs is grounded in the numerous tools that they put at SME retailers' disposal to overcome the challenge of competing against larger firms. We find that online marketplaces support SME retailers' business by supporting them

- To get online
- To grow online
- To be competitive online concerning cost, reach and innovation
- To overcome internal market frictions and sell cross-border
- To sell from remote locations

SME retailers learn from that symbiosis by building both business and reputation over time. Specifically, SME retailers can even leverage their reputation on online marketplaces by mirroring the experience on their own website shop, thereby become true multi-channel retailers and balancing the reliance on different channels.

Indeed, in any intermediation model (offline or online) a fundamental challenge for intermediaries is to stay relevant to the third parties exchanging information/opinions, services or goods (as in the case of online marketplaces). At any point in time, the seller and buyer can decide to move their transaction to a direct, non-intermediated transaction. This is a fundamental constraint on online marketplaces which implies that marketplaces strive to remain relevant, by offering:

- the most efficient and convenient way for retailers and consumers to transact and
- the widest possible range of shopping possibilities.

This explains why online marketplaces strive to foster the symbiosis with SMEs and maintaining the relevance, convenience and efficiency for both retailers and consumers to be on online marketplaces.

### **Online marketplaces help SME retailers start up online**

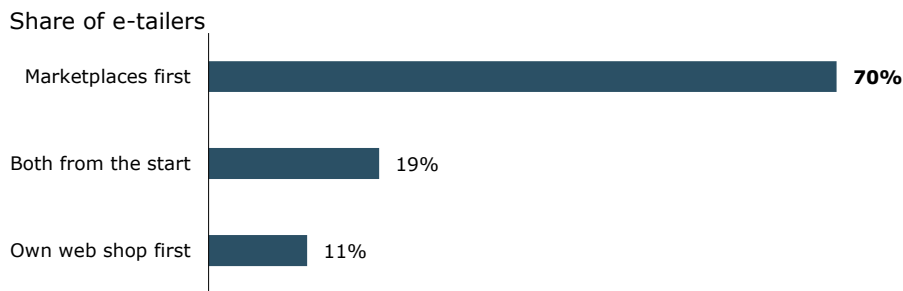
Online marketplaces play an important role in helping retailers to start up online. This is shown by a survey of German sports goods retailers that currently run their own website shop. In fact, 70 percent of those retailers stated that they started their business by using online marketplaces for most of their sales, see Figure 11.

Looking at all e-tailers, i.e., both those with an own website shop and those who do not yet have their own website shop, but sell on online marketplaces today, this percentage is likely to be even higher. In contrast, only 11 percent of e-tailers initially had most sales on their website shop. This low share is expected, due to the high costs associated with starting an online retail business on a retailer's own website shop compared to starting it on online marketplaces (see also Figure 11).

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**Figure 11 Marketplaces or website shop – what comes first? 2013**

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Note: Based on a questionnaire of German sports good retailers that run their own website shop.  
Source: Copenhagen Economics based on Sidley Austin (2013), p. 20.

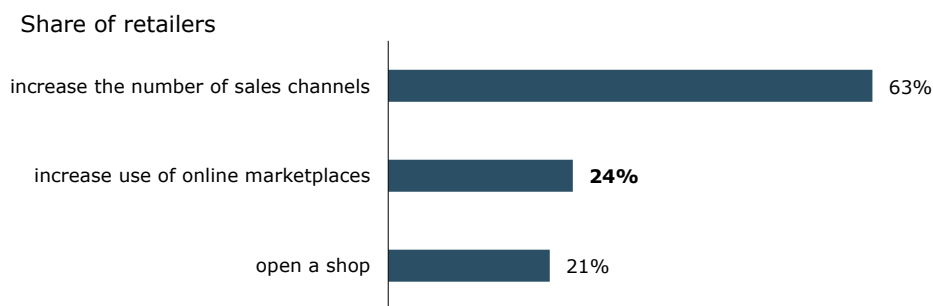
### **Online marketplaces help SME retailers grow online**

Online marketplaces are also perceived as a tool for growth by retailers. When asked about their strategy for growing in 2015, 24 percent of surveyed UK retailers stated that they planned to increase their use of online marketplaces, see Figure 12.

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**Figure 12 How to grow in the next year, 2014**

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Note: Based on a questionnaire of UK retailers.  
Source: Royal Mail (2015).

Moreover, as shown above, 63 percent of retailers consider an increase in the number of sales channels a way of growing. This demonstrates the value of a multi-channel strategy for retailers, of which the sale on online marketplaces is an inherent part.

**Online marketplaces support SME retailers to grow online and stay competitive online as to cost, reach and innovation**

Online marketplaces have become a popular tool for SME retailers to start up and grow online because they provide e-tailers lower cost, wider reach and participation in the mobile and other technological revolutions compared to selling via their own website shop, see Figure 13.

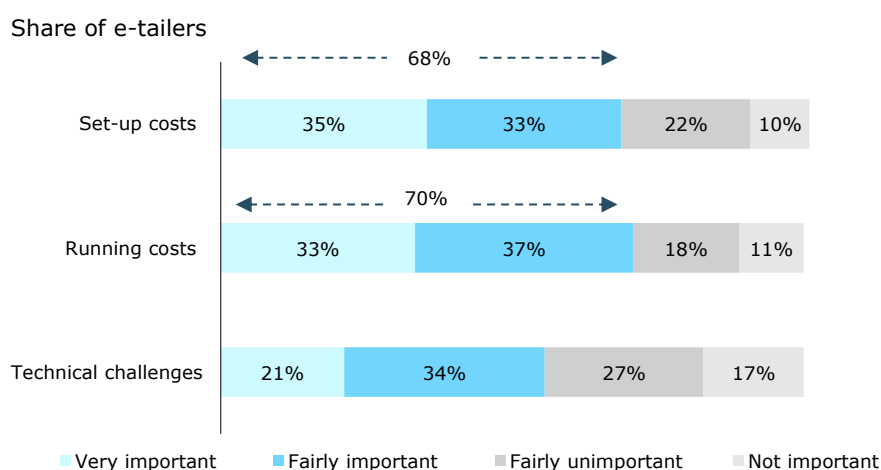
**Figure 13 Symbiosis between online marketplaces and e-tailers**

	<p><b>LOWER COST</b> Less costly way to set up and run an online business</p>	 <p>For <b>68%</b> of German retailers set-up costs are a fairly/ very important reason to not sell via an own website shop</p>
	<p><b>WIDER REACH</b> More traffic than on own website shop</p>	 <p><b>85%</b> of German retailers see lack of traffic as biggest hurdle for selling online via an own website shop</p>
	<p><b>MOBILE REVOLUTION</b> Only online marketplaces enable SME e-tailers to take part fully and efficiently</p>	 <p>Consumers will use a limited number of shopping apps from big providers Online marketplaces are currently the most popular shopping apps</p>
	<p><b>NEW TECHNOLOGIES</b> Online marketplaces offer SMEs access to new, disruptive technology</p>	 <p>Personalised shopping assistants via social media (e.g., eBay's ShopBot) Artificial intelligence to improve shopping experience (e.g., Etsy's Blackbird)</p>

Source: Copenhagen Economics based on various sources (see text below).

First, **cost** is a key reason for a retailer not to open its own website shop but instead make use of an online marketplace. In a 2013 survey of German retailers, 68 percent indicates that set-up costs for their own website shop are a fairly/ very important reason for them to not sell via an own website shop, i.e. for only selling online via online marketplaces, 70 percent of the surveyed retailers state that running costs are an important hurdle to operating their own website shop. In contrast, online marketplaces provide a less costly way to set-up and run an online business. On top of that, when starting up on online marketplaces, SME retailers do not need to acquire any IT expertise to launch a high-quality web-presence.

**Figure 14 Importance of cost for not opening an own online store**



Note: Sidley Austin survey of German e-tailers.

Source: Sidley Austin (2013), p. 18.

Second, while online sales theoretically allow all retailers to reach more consumers in more countries, this is not necessarily true in practice and even less so for smaller retailers. Even if SME e-tailers operate their own website shop, this may not be effective in marketing products beyond the perimeter of their brick and mortar store. This is because many smaller retailers cannot afford wide-reaching advertising campaigns and may find it expensive to buy search ads so to feature in the sponsored section of search engines results. Hence, it is not surprising that the **lack of traffic** is a key reason for retailers not to open their own website shop. In the same survey of German e-tailers, 85 percent of respondents saw the lack of traffic as the biggest hurdle for selling online via their own website shop.<sup>7</sup> Furthermore, a survey of German retailers showed that 83 percent of retailers consider online marketplaces an important building block for their business' success, since they can create a wider reach for their products.<sup>8</sup>

In contrast, SME e-tailers benefit from selling on online marketplaces since they can be more easily found by consumers, many of whom start their product search directly on the online marketplace (i.e., without even trying a search of their product via search engines).<sup>9</sup> On online marketplaces, retailers can then influence their ranking on the result list directly via, e.g., price level and good evaluations for previous transactions.

Third, only online marketplaces enable SME e-tailers to take part in the mobile commerce (m-commerce) revolution. M-commerce is a large and rising channel of online retailing. It accounted for 20 percent of e-commerce spending in Europe in 2015 (14 percent rise compared to 2014)<sup>10</sup>. The share of m-commerce in e-commerce is particularly high in the

<sup>7</sup> Sidley Austin (2013), p. 18.

<sup>8</sup> ECC (2016).

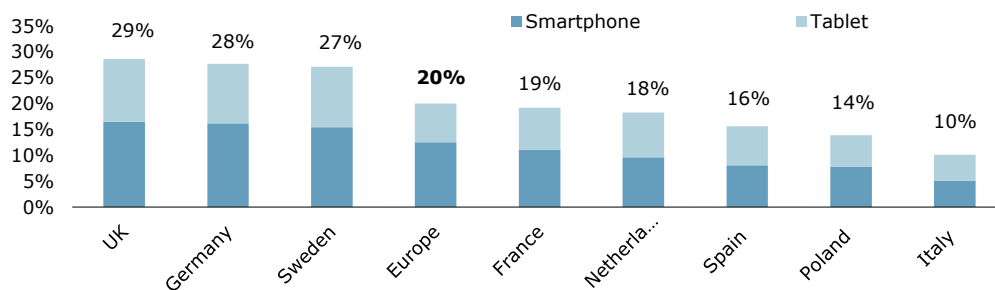
<sup>9</sup> Bundeskartellamt (2014), p. 3; Bundeskartellamt (2015), p. 30.

<sup>10</sup> EC JCR (Duch Brown and Martens) (2015), p. 7.

most mature e-commerce markets in the UK and Germany with close to one third of online retail sales taking place on mobile phones, see Figure 15.

While these figures indicate that m-commerce is important for sales, it might be even more important for ‘searches’, i.e. browsing the internet for products and good deals.

**Figure 15 Mobile commerce spending as share of total e-commerce, 2015**



Note: Graph covers total e-commerce, i.e. both goods and services sold online.

Source: Royal Mail (2015).

The spread of m-commerce means a challenge for smaller retailers in continuing to reach many consumers. First, building a well-functioning mobile app may be cost-prohibitive. Second, mobile shoppers tend to concentrate their mobile shopping activity on a limited number of mobile apps by bigger providers.<sup>11</sup> In contrast, consumers tend to download shopping apps by smaller retailers less frequently for convenience reasons. Hence, besides the cost associated with building an own well-functioning shopping app, small e-tailer apps might not be used. As a result, the more e-shoppers switch to shopping on mobile apps, the smaller the chances for small e-tailers to market their products to a wide audience of consumers.

In this situation, online marketplaces help SME e-tailers reach mobile shoppers, because their products will be automatically offered through the marketplace’s app. Currently, online marketplace apps are the most popular shopping apps. For instance, around 30 percent of German mobile users access eBay and Amazon via their mobile phones, see Figure 16.

<sup>11</sup> Bundeskartellamt (2015), p. 31.



**Figure 16 Use of eBay and Amazon by mobile users, 2014**

Note: Figure applies to Germany.

Source: comScore (2013).

Finally, online marketplaces offer SMEs access to new, disruptive technology. SME e-tailers automatically participate in every single one of the innovations launched by online marketplaces – innovations that they could not benefit from otherwise. There are several examples of innovations launched or planned by online marketplaces:

- **ShopBot:** eBay is currently testing a personalised shopping assistant called ShopBot on Facebook's messenger application;<sup>12</sup>
- **Blackbird:** Etsy has acquired Blackbird, using artificial intelligence to innovate on product searches on the marketplace through natural language processing, image recognition and analytics;<sup>13</sup>
- **Alexa Voice Service:** Amazon Echo provides via Alexa Voice Service a voice recognition service that consumers can use to add times to their to-do and shopping lists (this service is coming to the German and UK market in early 2017);<sup>14</sup>
- **Expertmaker:** eBay has recently acquired Expertmaker, a company that has created an advanced AI platform enabling optimization and automation, to apply its technology across the eBay platform, to help improve several aspects such as shipping and delivery times, trust and pricing;<sup>15</sup>

## 1.4 Online marketplaces help SME retailers sell cross-border

### SME retailers overcome internal market frictions and sell from remote locations using online marketplaces

Online marketplaces facilitate exports by even the smallest retailers. They reduce trade costs for SMEs and at the same time provide them with a global presence and reach previously reserved to large (multinational) retailers.<sup>16</sup> This enables SME retailers to benefit in

<sup>12</sup> Bloomberg Technology (2016).

<sup>13</sup> Techcrunch (2016).

<sup>14</sup> Amazon (2016).

<sup>15</sup> eBay (2016).

<sup>16</sup> WTO (2016), p. 54.

the same way of internationalisation (larger market, larger customer pool, less dependent on domestic economy) as larger exporting retailers.

The effects of reducing frictions can be striking. Lendle et al. estimate that the “distance effect” on trade flows (a measure of these frictions) is 65% smaller on eBay than for total trade due to the effect of an online marketplace like eBay in reducing information frictions associated with geographical distance.<sup>17</sup>

How can such a striking result be explained? In this section, we identify a number of factors that are drivers for cross-border e-commerce in the EU, but, if not functioning well, can constitute important frictions in the internal market. These frictions apply to both large and small retailers that would like to sell cross-border in the EU, but might be exacerbated for small e-tailers that face higher cost and reach-barriers to selling cross-border. We then analyse how online marketplaces help reduce each of these frictions.

**Table 1 Cross-border e-commerce drivers and frictions**

Drivers/ frictions	Consumers	SME e-tailers	Contribution of online marketplaces
Trust/ Experience	E-shopping experience Quality of goods Awareness of cross-border consumer rights	Branding possibility Online selling experience	<ul style="list-style-type: none"> <li>• Create consumer trust for retailers from other countries</li> </ul>
Geography/ Culture	Home market size Language Home bias	Home market size Language	<ul style="list-style-type: none"> <li>• Consumers/ retailers are no longer dependent on the size of their home markets</li> <li>• Multi-language service system for CB sales facilitate cross-border sales</li> </ul>
Technological development	Broadband penetration Digital skills	Broadband penetration Digital skills	<ul style="list-style-type: none"> <li>• Same effect as other online channels</li> <li>• Easier to reach mobile broadband-only consumers</li> </ul>
Operational conditions	Delivery times	Delivery logistics	<ul style="list-style-type: none"> <li>• Shipping aid programmes facilitate delivery logistics for e-tailers</li> <li>• Online marketplaces can reduce delivery cost/ prices by aggregating SME demand for delivery services</li> <li>• Different online marketplace business models available for SMEs to choose (e.g., fulfilment)</li> </ul>

Source: Copenhagen Economics.

### Closing the trust and experience gap

Experience and trust are strong drivers of e-commerce engagement. A lack of trust and concerns about, e.g., safety of website payment or the quality of products sold by e-tailers from other EU countries might prevent consumers from shopping online cross-border.<sup>18</sup> This means that an e-tailer from, for instance, Portugal, might forego a sale to a German consumer, because the consumer does not trust that payment on the e-tailers’ website shop is sufficiently safe. Online marketplaces close this trust-gap by connecting consumers with retailers from different countries in one trusted location, thereby giving e-shoppers the confidence to purchase from an unfamiliar, foreign retailer. When shopping on

<sup>17</sup> Lendle et al. (2013).

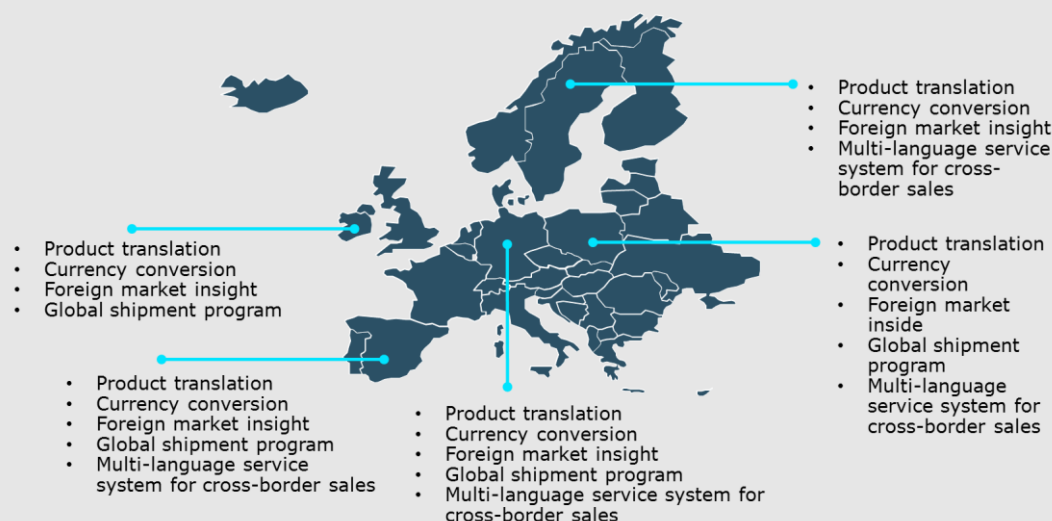
<sup>18</sup> IPC (2013), p. 17; Bundeskartellamt (2014), p. 4.

their habitual online marketplaces, consumers trust the purchase and payment process, have return guarantees and can resort to resolution mechanisms in case of conflict. Moreover, the review and rating mechanisms for e-tailers offering products on the online marketplace builds consumers' trust in the quality of the products they purchase and the reliability of the seller. In turn, e-tailers can gain consumer trust through consumers' existing confidence in the marketplace.<sup>19</sup>

Experience plays a role for SME e-tailers that often start by selling on their domestic market before 'going abroad'. The lack of specific capacities (e.g., to translate websites) and expertise (e.g., of different VAT systems, different consumer rights) required for selling cross-border can prevent particularly small enterprises from selling online cross-border. Online marketplaces can solve part of these experience problems for e-tailers from day one: retailers that want to increase their sales in other EU member states can do so without incurring the cost of launching a dedicated website shop in a different language. Furthermore, online marketplaces facilitate cross-border sales insofar as they provide retailers with special services designed to increase their foreign market insight and ease currency conversion and translation. They also often provide guidance and information on the applicable rules when selling cross-border, see Box 1.

### Box 1 Trade facilitation services offered by online marketplaces

Sellers in Ireland, Spain, Germany, Sweden and Poland, for instance, benefit from the following services by online marketplaces geared at making cross-border sales easier and less cumbersome.



Source: Copenhagen Economics based on Allegro, Amazon (2016), Ebay (2016), Fruugo (2016), Miniinthebox (2016).

<sup>19</sup> Bizrate Insights/Forrester (2012), p. 1.

### **Geography/ Culture**

The size of a country's home market determines to what extent consumer and retailers are dependent on cross-border sales for their purchases (e.g., in terms of number of products available on the home market) and sales (e.g., in terms of the size of the home market). Consequently, smaller countries tend to have a higher share of cross-border sales.<sup>20</sup> When selling on online marketplaces consumers and retailers are no longer dependent on the size of their home markets. In addition, as discussed above, language barriers greatly determine the extent to which cross-border sales and purchases take place between countries. The multi-language service system offered by many online marketplaces facilitates cross-border sales. An eBay experiment in the city of Mönchengladbach in Germany shows how online marketplaces enable cross-border sales, see Box 2.

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### **Box 2 eBay's Mönchengladbach experiment**

Online marketplaces offer retailers the opportunity to reach at low cost a huge number of potential customers outside of their home country. In a recent eBay pilot in the German city of Mönchengladbach, which started in October 2015, 79 local sellers joined eBay en-masse as a neighbourhood to sell online. Since the start of this project, the merchants have sold goods into more than 84 countries.

Source: Copenhagen Economics based on eBay material.

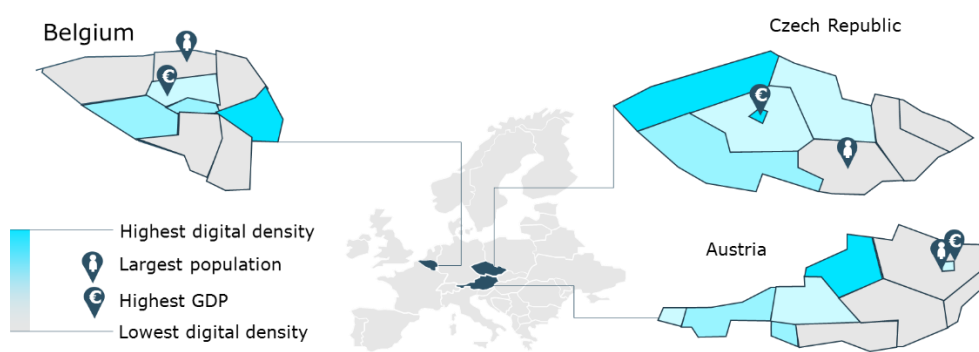
A further element related to geography is that large (online) retailers have an incentive to locate in larger countries where the market is biggest. Particularly brick and mortar retailers will choose to locate in the economic centres of the country where they expect the strongest demand. In turn, online marketplaces help small retailers to operate out of remote locations of the EU, even if they are characterised by low population density and/or, low GDP per capita while still reaching a wide array of customers. This fosters more decentralised, inclusive economic growth, see Box 3.

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<sup>20</sup> Copenhagen Economics (2016), p. 16.

### Box 3 Inclusive economic growth through online marketplaces

An eBay analysis of digital density of SME e-tailers shows that the regions with the highest digital density of SME e-tailers are not necessarily the regions with the highest GDP or largest population. This shows that online marketplace activity is more dispersed, i.e. less concentrated than traditional economic activity, allowing for more inclusive economic growth.



The digital density of SME e-tailers measures how densely a region is populated by successful SME e-tailers. This indicator combines (i) the number of eBay SMEs per 100,000 inhabitants and (ii) the sales by eBay SMEs per 100,000 inhabitants in a given region. Per country, digital density measures how a region performs against the national average digital density.

Source: Copenhagen Economics based on eBay (2015).

#### Technological development

While online marketplaces depend on broadband penetration in the various countries and digital skills of consumers in the same way as other online retail channels, they do make a difference for mobile-only consumers, i.e. consumers relying more on their mobile internet connection than on their broadband connection when shopping online at home.

Moreover, in some areas – especially with the completion of roll-out deployment of 4G mobile networks across European countries, consumers rely on a better mobile internet connection than what they can achieve via fixed broadband. Those consumers might be more inclined shop online via a mobile app. In this case, apps by online marketplace offer a useful one-stop shop for consumers while allowing smaller e-tailers to reach this group of consumers.

#### Operational conditions

Operational considerations relating to delivery and logistics influence the development of cross-border e-commerce. Consumers might be discouraged from shopping cross-border when they expect delivery to take long or to be complicated and expensive.<sup>21</sup> In turn, small

<sup>21</sup> According to the European Commission, “a good example is long delivery time, which is the most commonly experienced problem (17%) amongst those who experienced problems [when purchasing online cross-border], equally reported by 18% of EU28 online respondents as a major concern to their domestic online purchases” (EC, 2015, p. 183).

e-tailers might be discouraged from selling cross-border when they cannot identify reliable logistics and distribution solutions or fail to receive delivery solutions at competitive prices.

Online marketplaces facilitate delivery logistics for e-tailers through shipping aid programmes. Different online marketplace business models are available for SMEs to choose from, depending on their preferences concerning fulfilment. Furthermore, online marketplaces often aggregate SME demand for delivery services allowing them to get better delivery deals for SMEs. This reduces delivery cost for SMEs, making their package of product and delivery more competitive both compared to larger e-tailers and domestic e-tailers.

### **Conclusion: Contribution to SMEs' competitiveness**

Large retail platforms and service providers such as Amazon, eBay and PayPal now provide or are developing ancillary services and payment systems to facilitate exports by even the smallest sellers. Such online marketplaces can offer SMEs a means to scale up at minimal cost, providing nearly instant solutions that include secure payment systems, logistics support, and global visibility of the kind once reserved for large firms.<sup>22</sup>

International organisations (e.g., WTO, OECD, UNCTAD and ITC) promote online marketplaces as a powerful tool for facilitating exports for SMEs. Governments in developing countries have recently embraced the use of online marketplaces as a way to bring their SMEs on global markets. Hence, the use of online marketplaces as an enabler for exports for EU SMEs is crucial to ensure SME's competitiveness in the long term.<sup>23</sup>

The factors presented above are demonstrated in the day-to-day experience of online sellers that choose marketplaces as a valuable tool to enhance their business. The two following small business founders show how valuable online marketplaces are as a channel of business growth.

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<sup>22</sup> WTO (2016), p. 50.

<sup>23</sup> See for instance, WTO (2016).

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## Box 4 Recognising the value of the marketplace channel

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### **Andreas Müller, Deltatecc GmbH, Germany**

Andreas Müller, founder of one of the most successful online retail companies in Germany, illustrates the potential of online marketplace to grow businesses and to create jobs.

Originally Andreas only sold a single product - cell phones - online, but with the help of online marketplaces his company now offers everything from electronics to home appliances and kitchen accessories. This expansion was directly enabled by the use of online marketplaces, which allowed the business to reach a wide range of customers at low cost. According to Andreas, for SMEs, this is the most crucial feature of online marketplaces.

Andreas is convinced that that reaching mobile app users constitutes a major benefit of using online marketplaces.

In turn, Andreas points out that online market bans would seriously endanger his business and the jobs of his 55 employees.

Source: Copenhagen Economics based on e-tailer interview.

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## Box 5 Selling cross-border from a remote location

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### **Mario Calabrese, Footlover, Italy**

With the help of online marketplaces Mario Calabrese, a third generation shoe-maker from Italy, exports 50% of his production cross border to countries as far away as Australia and the USA.

Even though Mario lives in a small and remote community in southern Italy, he can use online marketplaces to offer his products to customers around the globe. Entry barriers are low and online markets provide him with the necessary tools to service his international customers. In addition, selling online has significant spillover effects for his two physical retail stores as he now participates in global commerce thanks to business contacts and relationships he established while selling online.

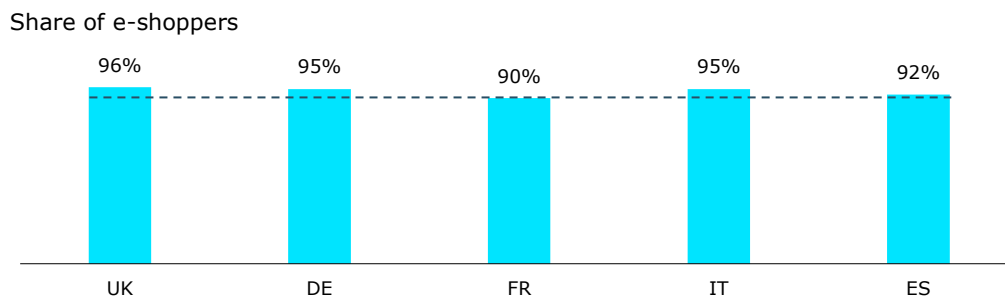
His success, however, was impaired by bans prohibiting him from selling online from brands he has worked with for 25 years. These bans resulted in a loss of 50 percent of his sales. Even after the bans were lifted the damage persisted, as the turnover in the following four years struggled to recover.

Source: Copenhagen Economics based on e-tailer interview.

## 1.5 Consumers benefit from online marketplaces

Online marketplaces are important for consumers. Over 90 percent of surveyed shoppers in European countries shop with online marketplaces, see Figure 17. Online marketplaces are the preferred shopping channel for many e-shoppers.

**Figure 17 Do you shop on online marketplaces?**



Source: Morar (2016) e-tailer survey.

Online marketplaces benefit consumers in a way that other channels do not, for several reasons.

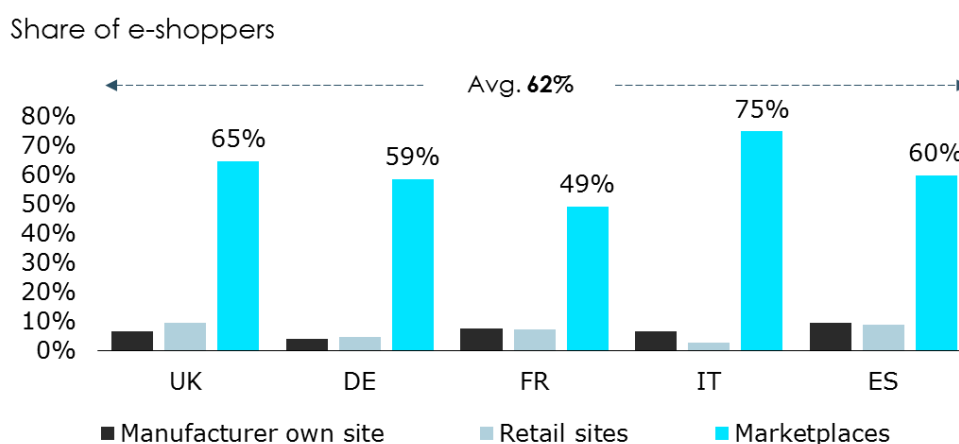
First, consumers benefit from lower prices on online marketplaces. A 2008 study of eBay average price savings demonstrates that, across the UK, Germany and France and across several product categories, consumers save on average 17 percent when buying on the eBay online marketplace compared to a retail store.<sup>24</sup>

This corresponds to consumers' own perception of getting better prices on online marketplaces. 62 percent of respondents to a consumer survey spanning several European countries believe that the best prices are available on marketplaces, see Figure 18.

<sup>24</sup> Frontier (2008), p.19.



**Figure 18 Which online retail site gives consumers the best price available?**



Source: Copenhagen Economics based on Morar (2016) e-shopper survey.

Moreover, according to a 2016 survey of consumers of electronics 70 percent of respondents find products on online marketplaces cheaper than on websites of specialists or generalist retailers.<sup>25</sup>

Second, consumers benefit from more choice on online marketplace than on other distribution channels. The same survey of consumers of electronics finds that 80 percent respondents consider that online marketplaces provide more choices than physical stores while 69 percent consider that online marketplaces provide more choices than specialist retailers online.<sup>26</sup>

Third, consumers benefit from lower search costs<sup>27</sup> and higher convenience of use and time efficiency when shopping on online marketplaces.

This is important, since not every way of purchasing is equal for consumers. For the same good, brand sold and for equal prices and quality, the most convenient shopping experience delivers the highest consumer surplus, leading to higher social welfare. Channels and ways of purchasing products differ as to the convenience of the shopping experience they deliver for consumers.

Consumers use their time better when e-shopping on any kind of platforms. This applies especially to shopping via mobile apps.

<sup>25</sup> Compass Lexecon (2016), p. 11.

<sup>26</sup> Compass Lexecon (2016), p. 14.

<sup>27</sup> We define search costs as the costs involved for the consumer in searching different products and services.

Evidence from empirical literature shows that, all else equal, consumer surplus is larger for online marketplaces due to a reduction in search costs. In particular, online marketplaces are considerably frictionless in regards to search costs. Lendle et al. show that search costs are greatly reduced on the eBay online marketplace.<sup>28</sup>

Furthermore, when sellers and buyers transact (offline and online), typically so-called matching costs occur, whereby both buyers and sellers face a risk that the other party 'does not comply', i.e. does not pay, does not deliver etc. On online marketplaces these risks are mitigated by guarantee schemes, online resolution procedures and feedback forums with rating systems.

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<sup>28</sup> Lendle (2013) pp. 3; 12-14.

## Chapter 2

# Economic detriment from online marketplace bans

Online marketplace bans are today a widespread and rising practice that affect e-tailers of all sizes, in many EU countries and across many product categories to a similar, strong extent. Yet, it is especially SMEs that suffer, since online marketplace bans disable a retail sales channel that has become important for both SME e-tailers and their consumers.

Online marketplace bans harm small e-tailers in many ways. The most immediate effect of online marketplace bans lies in decreased sales revenue for e-tailers selling on online marketplaces. SME e-tailers indicate that they stand to lose 53 percent of their total online revenue from pervasive online marketplace bans. This is supported by analysis of e-tailer sales revenue on the eBay online marketplace. Beyond this, SME e-tailers' long-term customer relations and profitability are put at risk when online marketplace bans are imposed.

Moreover, were online marketplace bans to be applied pervasively, this would undermine the key benefits that online marketplaces present to SME e-tailers, such as starting up and getting online as well as benefiting from the boom in mobile commerce. Online marketplace bans are likely to counteract the cross-border sales development that SME e-tailers have achieved thanks to online marketplaces. Consequently, such bans impair the EU policy aim of a frictionless, ever more deeply integrated Digital Single Market.

Online marketplace bans impact consumer welfare by taking away the convenience-enhancing features that online marketplaces present to consumers concerning the ease of search, transparency and time efficiency of the purchase.

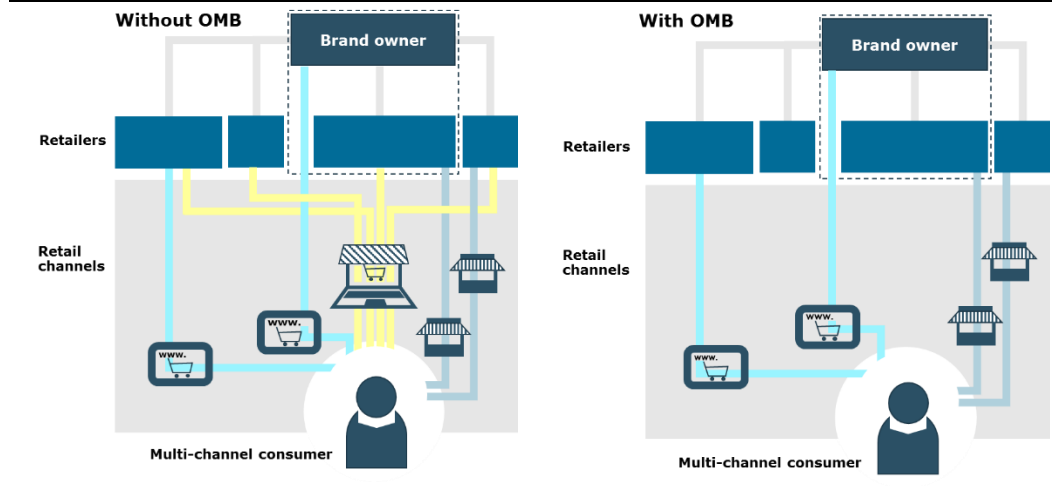
We find that online marketplace bans lead to a restriction of competition between retailers of the same brand (intra-brand competition) that cannot sufficiently be outweighed by competition between brands (inter-brand competition) nor the unsupported efficiency gains arising from these bans.

Unless EU institutions send a clear signal that online marketplace bans are not permissible, this would likely lead to an increased use and enforcement of these bans by brand owners. As a result, in a scenario where online marketplace bans become pervasive, this would create a strong impediment to SME e-tailers. This would cause a major upheaval in retail commerce, depriving e-tailers of an estimated €26bn of online retail sales, diverted elsewhere.

This chapter illustrates the functioning of online marketplace bans and analyse their economic impact on consumers, SME e-tailers and competition.

### 2.1 Policy context and functioning of online marketplace bans

Online marketplace bans are restrictions mostly imposed in selective distribution agreements whereby a brand owner disallows the sale of its brand on online marketplaces. In other words, the retailer can no longer offer the brand on online marketplaces and is thus restricted to marketing the brand on its own online shop and/or brick and mortar store.

**Figure 19 Retail before and after an online marketplace ban**

Source: Copenhagen Economics.

Besides the competition effects balance analysed below in this section, online marketplace bans have an impact for consumers and retailers.

For consumers, online marketplace bans mean that one sales channel will be blocked for the purchase of the brand: consumers have less retailers to choose and compare prices from and are no longer true multi-channel consumers. When a consumer can no longer find the brand she intended to buy on the online marketplace, she can react in several ways:

- stay on the marketplace and opt to buy a product from another brand; or
- leave the online marketplace in order to purchase the banned brand via another channel (e.g., the online website shops of retailers or in a brick and mortar store); or
- not make a purchase in that instance.

For e-tailers, an online marketplace ban can have different effects depending on the reactions of consumers. An e-tailer that previously sold the brand on online marketplaces will no longer be able to do so and will lose the sales of that brand. This e-tailer might be able to mitigate the effect of the ban by selling a second brand to the consumer or by recouping some of the lost sales via sales of the first brand on other channels, e.g. on its own website shop or brick and mortar store. This option is, of course, only open to an e-tailer that does not only sell via online marketplaces and whose website shops/ brick and mortar store is sufficiently known by consumers. Some retailers might also benefit from an online marketplace ban: these are likely to be large retailers or the brand owners' retailing arm which are not present on online marketplaces and whose websites and stores hold sufficient prominence with consumers.

In this chapter, we will analyse how widespread online marketplace bans are in the EU and investigate in detail their impact on SME e-tailers, consumers and competition. We start below with an explanation of why competition concerns arise in this area.

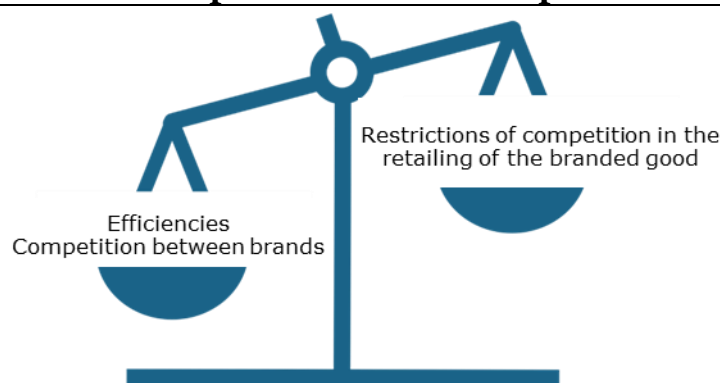
### Selective distribution agreements have by nature anti-competitive effects

When applying online marketplace bans, brand owners typically do so by introducing the ban as a restriction within a selective distribution agreement. Brand owners typically use selective distribution arrangements to gain greater control over the way in which their products are distributed by retailers. In a selective distribution system the brand owner agrees to supply only to retailers (distributors) who meet certain minimum criteria related to the maintenance of a certain product image or level of service quality. In essence, with a selective distribution agreement, a brand owner determines who can sell their brand, where and how.

Competition law has always been somewhat concerned with selective distribution agreements. Selective distribution agreements *restrict competition between retailers* on the same brand, by restricting the overall number of retailers that sell the product and by restricting the mode of sale. Therefore, selective distribution agreements have, by their very nature, some anti-competitive effects.<sup>29</sup>

Given the anti-competitive effects associated with such agreements, the relevant question under competition law is then whether these anti-competitive effects are counter-balanced by some other positive effects resulting from selective distribution agreements. When past regulation, guidance and competition case law has accepted selective distribution agreements, it has been based on a belief of a positive balance of net effects, see Figure below.

**Figure 20 Conditions for selective distribution agreements to be acceptable from a competition effects viewpoint**



Source: Copenhagen Economics.

As shown above, a first factor in the overall balance of effects is that selective distribution agreements (and thus also online marketplace bans which are specific conditions that

<sup>29</sup> A separate, yet related, class of agreements are exclusive distribution agreements. These agreements may include territorial restraints, implying that a retailer cannot actively market the brand in question in certain parts of the country or in certain countries, but it is restricted to marketing it on a confined territory. This traditional restriction of markets country-by-country is a practice akin to what today is referred to as geo-blocking in digital markets.

brand owners have introduced on top of these agreements) have a restricting effect on competition. This is the primary source of concern when assessing these agreements.

A factor reducing concerns is that, only if there is sufficiently fierce competition *between brands* (so-called inter-brand competition), might the overall restrictions on competition resulting from selective distribution agreements be limited.

An additional factor reducing concerns is that economic theory has traditionally justified selective distribution agreements as a way to *increase efficiency* in the distribution of the branded goods by, for instance:

- Mitigating market failures due to information asymmetry (consumer vs brand owner; brand owner vs retailer)
- Avoiding free-riding by retailers not investing in showcasing products, thus aligning incentives of retailers closer to those of brands/brand owners
- As a result, supporting competition on quality factors

Brand owners have stressed the importance of efficiencies arising due to selective distribution agreements, as summarised in the box below.

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### **Box 6 Selective distribution agreements: Brand owners' alleged benefits**

According to economic theory, from a brand owner's point of view, there can be several rationales for setting up a selective distribution system:

- **Brand owner monitoring of high quality retail services:** The brand owner is interested in having retailers that provide consistent, high quality services (e.g., pre- and post-sales services) to consumers, however visiting and monitoring stores at all times is too costly to be efficient and can only be done in a limited basis. This results in asymmetric information: the retailer knows its service quality, while the brand owner does not fully observe the actual service level provided by a retailer. Thus, there is a risk that this asymmetric information might reduce retailers' incentives to provide service, thus leading to overall lower service levels and reduced sale of the brand owner's product.
- **Prevent free-riding by low service quality retailers:** Consumers require information to decide their purchases. If only some but not all retailers invest in activities promoting the brand owner's product (e.g., in conveying of information to the customer, sales personnel training, displaying the product, etc.) there is a risk that other retailers free-ride on these investments and (not incurring the related costs) are able to offer the product at a cheaper price and/or higher retail margin. The risk is then that consumers benefit from the information, high-quality product presentation and services at a 'premium retailer' that has made the necessary investments but then buy the product at the cheaper retailer (a practice labelled as "showrooming"). This would lower the premium retailers' incentives to provide a high service levels, thus lowering overall service level, brand image and the branded good's sales. If the brand creates rules that avoid free-riding, it protects the retailers' investments, which are then more likely to stock that brand.
- **Softening inter-brand competition:** Vertical restraints, e.g. which sales channels are made available, can reduce transparency and thereby reduce inter-brand competition. This is particularly relevant if there exists a network of similar contracts, e.g. if multiple producers simultaneously apply online marketplace bans.

Source: Copenhagen Economics.

### Online marketplace bans: no net benefit expected

Before the advent of the internet, consumers essentially purchased their products mainly via transactions in brick and mortar stores (with limited distance selling). Retailers used mainly the brick&mortar channel to market brand-owners' products. As considered in the previous section, selective distribution agreements, and the quality criteria applied by brand owners therein, were considered to be a way to foster retail efficiencies by improving coordination between the brand-owner and retailers, so to mitigate problems due to free-riding and information asymmetry. The efficiencies accruing from selective distribution agreements were defined on that basis and presumed to outweigh the innate anti-competitive effects of selective distribution agreements.

In this section, we consider whether the general conclusion as to the favourable net balance of competition effects for selective distribution agreements should apply also for the specific case of the online marketplace bans contractual restrictions. This is a key question, since the advent of the internet has revolutionised the retail sector. As a result, the rationale for accepting online marketplace bans may not be valid today.

In what follows, we identify key changes across the retail value chain due to the advent of the internet and find that these changes have likely altered the balance of effects. As a result, it cannot be taken for granted that online marketplace bans, simply by being a condition attached to selective distribution agreements, have the same positive net balance of effects traditionally associated to selective distribution agreements.

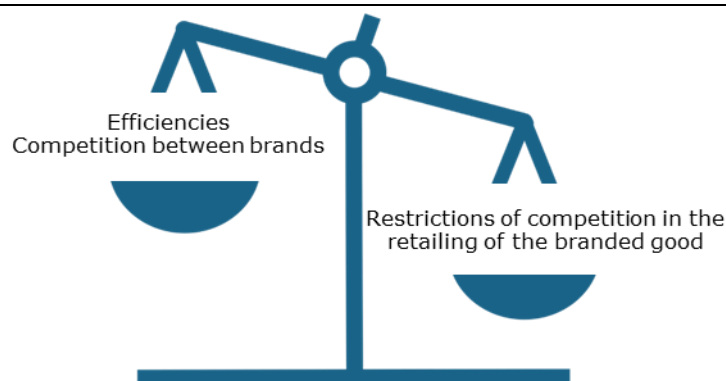
On the contrary, when we apply to the specific case of online marketplace bans the same framework used in the past to evaluate conceptually selective distribution agreements, we find that the net balance of competition effects is likely negative for online marketplace bans, for two reasons:

- Curtailed efficiency benefits
- Increased significance of impact on restricting retailing competition

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### Figure 21 Online marketplace bans: likely negative balance of competition effects

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Source: Copenhagen Economics.

### Curtailed efficiency benefits

We have identified three reasons why in the case of online marketplace bans, a justification based on efficiency benefits is curtailed:

1. The internet allows brand owners to monitor easily retailers, reducing the information asymmetry
2. The internet enables consumers to obtain information on products independently from retailers' efforts, thus reducing free-riding incentives
3. Consumers combine information from online retailers and brick&mortar retailers

#### *1. The internet allows brand owners to monitor easily retailers, reducing the information asymmetry*

Selective distribution agreements were designed to prevent one store free-riding on the quality of service and presentation of others. Before the internet, when retail was mainly brick&mortar retail, monitoring involved store visits, i.e. high costs for the brand owner, thus resulting in incomplete information about the service level offered by retailers.

Instead, for any online retail outlet (whether an e-tailer's own website store or its store on an online marketplace) the internet allows brand owners to monitor and control free-riding by retailers. Issues may persist with brick&mortar retail activities, where the internet does not make it easier for brand owners to monitor the retail service quality.

Online marketplace bans are targeted at online sales. Yet, online is the retail channel where the information asymmetry problem – the source of the traditional efficiency justification for selective distribution agreements – is now addressed by the advent of the internet. Thus the efficiency rationale of online marketplace bans is curtailed.

#### *2. The internet enables consumers to obtain information on products independently from retailers' efforts, thus reducing free-riding incentives*

In addition, quality retail service level was traditionally meant to ensure that consumers could receive information necessary to decide what to purchase. The value of competition over quality will be the larger, the more consumers are dependent on the retail activity to provide information to them.

While in the past the only way for consumers to orient themselves was to experience goods in store, today with the internet consumers can and do research and easily obtain relevant information online, independently from the effort of retailers. With the advent of the internet (which includes generalist search engine, review websites, social networks and other information dissemination and retrieval tools), consumers' information starting point and potential is much enhanced compared to before the internet.

As a result, the welfare benefits of the retailers' traditional service activities are reduced. Moreover, the value that a consumer derives from free-riding by visiting a high-service level retailer and then purchasing at a low-service retailer are reduced. Thus also the efficiency rationale of online marketplace bans is curtailed.



### *3. Consumers combine information from online retailers and brick&mortar retailers*

A key traditional rationale for justifying selective distribution arrangements was to curtail the consumer practice of “showrooming”, i.e. obtaining information on the good at a premium retailer while buying at a discount retailer (which was free-riding on the information and service provided by the first retailer). If applying this logic to the assessment of online marketplace bans, this justification would apply if there to be a one-directional pattern of consumers obtaining first information in brick&mortar stores and then making purchases on retailers’ stores on online marketplace.

However, in practice this is not the case. Consumers have become truly multi-channel consumers and they combine information on goods from both physical and online retail interactions in order to make their purchase decisions and then purchase the brand either online or in a physical brick and mortar store.

Even when consumers get information from one retailer and buy at another, empirical studies have established that this behaviour is broadly balanced across both flows. As found by the Compass Lexecon (2016) survey, the share of consumers documenting oneself by visiting a brick&mortar store and then shopping at an online retailer is similar to the share of those doing the converse: documenting oneself at an online store and then purchasing at a brick&mortar store. The survey finds that 56% of consumers research consumer electronics products online but then buy the products in a physical store (“webrooming”), as opposed to 49% who research the products in a physical store and then buy them online (“showrooming”).

Therefore, since “showrooming” is met by an equivalent or even larger amount of “webrooming”, the free-riding justification is not a strong rationale to support online marketplace bans.

### *Conclusion on the efficiency justification of online marketplace bans*

The advent of the internet has led to a reduction in information asymmetries and free-riding issues, reducing the overall welfare benefits associated in theory with a contractual restriction such as an online marketplace ban.

This conclusion is without prejudice to the merits of other types of contractual conditions. Brand-owners can set transparent and non-discriminatory criteria for the distribution of their brands online (as they can do offline), criteria that are objectively and directly related to enhancing the quality of the consumer experience.

Most notably, this leaves unchanged the opportunity for brands and manufacturers to compete over the quality attributes of the product itself. Indeed, with the advent of the internet, brands and manufacturers can be ever more confident that online information resources allow quality products to be known to and recognised by consumers.

### Increased significance of impact on restricting retailing competition

The advent of the internet is revolutionising retail value chains. Brand owners have responded by adopting new legal and commercial strategies.

Some brand owners' response has been to impose restrictions on all online sales altogether, which was found unlawful under competition law in the Court of Justice EU Pierre Fabre case. Other brands reacted by imposing online restrictions just on sales via online marketplaces, i.e. online marketplace bans.

Another facet of the internet revolution is that it makes it easier and cheaper for brand owners to retail directly to consumers, via their own brand website stores. This form of vertical integration was possible also in the past via brick&mortar stores, albeit then as a more expensive and cumbersome strategy for a brand owner. Thus many brand owners have started their own online retail operations in order to reach consumers directly online, in a way not intermediated via independent retailers. Hence, today it is increasingly commonplace for independent retailers to face direct competition from brand owners at the retail level.

Many brand owners are thus today vertically integrated, implying that they supplying retailers but also competing with them at the retail level. This is a similar situation as the situation in which – for instance in infrastructure / network industries – concerns arise for dominant players as to abusive margin squeeze or anti-competitive practices imposed by a vertically integrated company aiming to foreclose its downstream competitors.<sup>30</sup>

The vertically integrated brand owner has fundamentally different incentives than a brand owner not present at the retail level. This is because the brand-owner now does not solely focus on the wholesale price it receives for its products from retailers but also cares about its market position, prices and volumes at the retail level.

This raises the significance of the original competition concerns associated with a practice such as an online marketplace ban. Vertical integration of the brand owners implies that the impact of online marketplace bans on restricting retailing competition is more significant, due to the direct competition between the brand's own online website store and the independent retailers' outlets.

## **2.2 Online marketplace bans are more and more widespread**

Today, online marketplace bans are widespread. They affect retailers in many EU countries, of many sizes and across many product categories.

A survey conducted by Choice in eCommerce among over 7,000 retailer in Europe has yielded a list of over 2,000 brand owners that implement restrictions to online retail trade many of which are market-place bans.<sup>31</sup> Competition authorities have intervened a number of cases, of which some are listed in Table 2.

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<sup>30</sup> While the relationship is conceptually similar, a distinction is that brand owners, even insofar as they possess market power, may not be dominant undertakings.

<sup>31</sup> See Choice in eCommerce (2016).

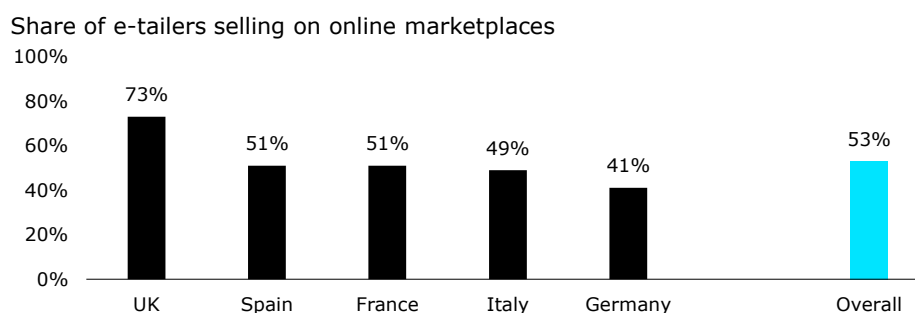
**Table 2 Online marketplace bans subject to competition law investigations**

Brand	County	Time frame	Product category
Deuter	Germany	2013-2016	Outdoor equipment
Ping	United Kingdom	2016	Golf equipment
Adidas	Several countries	2012-2015	Running shoes
Sennheiser	Germany	2013	Headphones
Samsung	France	2012-2014	Televisions

Note: Ping imposes an ban of online sales, which, de facto, results in a ban of online marketplaces.

Source: Copenhagen Economics.

It is important to note that the relevant figure to look at when assessing the spread of online marketplace bans is their spread among those e-tailers that sell on online marketplaces, see Box 7. A recent Morar October 2016 survey finds that, across large EU countries, the share of relevant retailers who are affected by online marketplace bans today amounts to over 50 percent, Figure 22. The survey also shows that the impact of online marketplace bans is not an exclusively German phenomenon, but that retailers are affected to a similar or larger extent in other EU member states.

**Figure 22 Retailers subject to online marketplace bans, 2016**

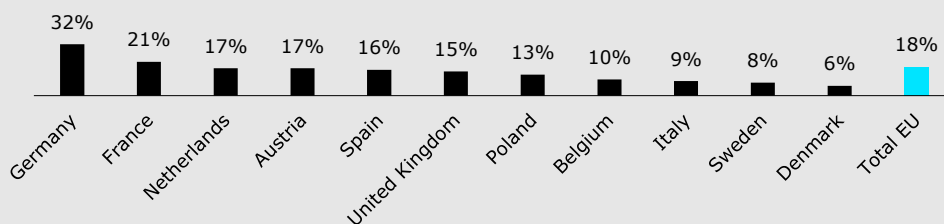
Source: Copenhagen Economics based on Morar (2016) e-tailer survey.

### Box 7 Assessing the spread of online marketplace bans

The European Commission E-commerce sector inquiry reports that 18% of all retailers across the EU are subject to online marketplace (OM) bans. However, this is based on the sample of respondents to the EC consultation, which inherently reflects differing ability across firms to engage in a consultation response (very small firms, many of which sell online using OMs often do not have the resources to respond to a large consultation). Moreover, a respondent’s awareness to the presence of OM bans may depend on whether the respondent’s firm is active on OMs or not. A retailer that does not sell via OMs may not recall that an OM ban is written into its selective distribution agreement – or at least not be aware as much as a retailer that, on the contrary, is active on OMs. It is notable that only “around a third of respondent retailers are selling via a marketplace” (EC, 2016A, p. 33).

#### Retailers subject to online marketplace bans

Share of all retailers



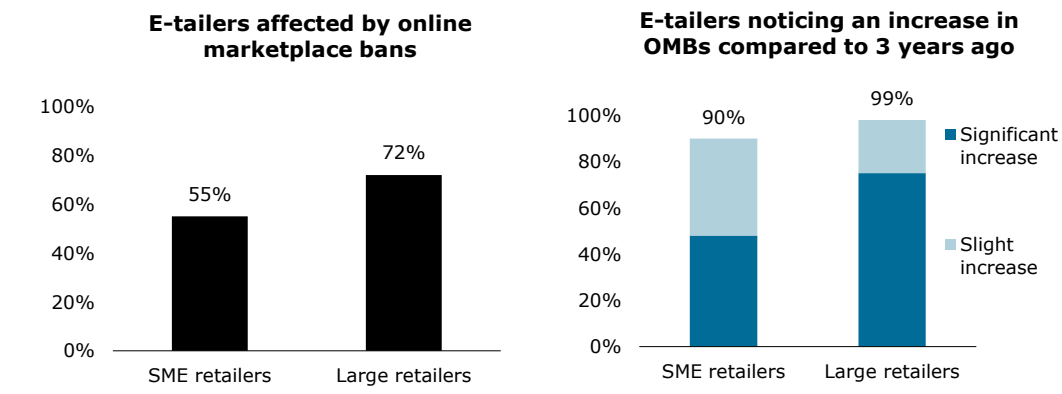
Source: European Commission (2016 A), Fig. B.64, p. 145.

Thus, it is likely that the share of retailers that is *affected* by OM bans is higher than the above 18% figure. In the (extreme) scenario where it is only the retailers selling on OMs that recalled and reported the existence of OM bans, this would imply that the 18% reported share corresponds to a 60% share (18% divided e.g. 30%), over the wider sample. We note that the statistics found in the Morar (2016) specific e-tailer survey was 53%.

Source: Copenhagen Economics.

Among SME retailers selling on online marketplaces, 55 percent indicate that they are affected by online marketplace bans and 90 percent have noticed an increase in online marketplace bans in the last three years, see Figure 23. Among larger retailers online marketplace bans are perceived as even more pervasive, with 72 percent indicating that they are affected and 99 percent perceiving a rise in bans during the past three years.

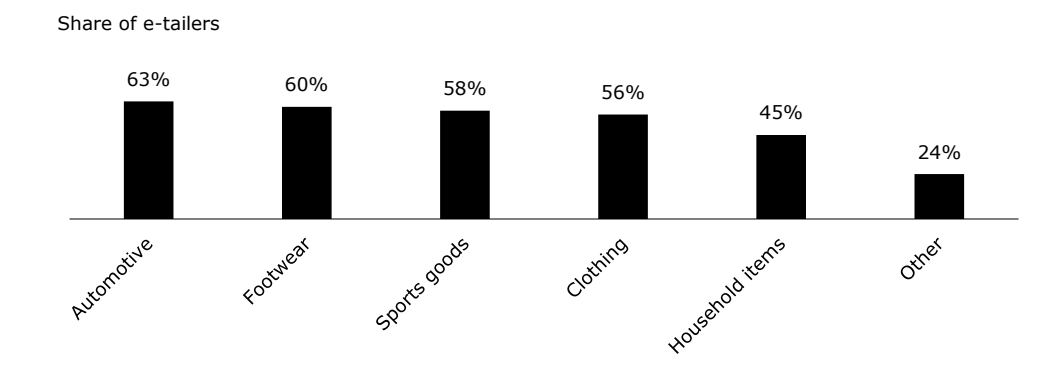
**Figure 23 Retailers affected by online marketplace bans, 2016**



Note: applies to e-tailers selling on online marketplaces.  
 Source: Copenhagen Economics based on Morar (2016) e-tailer survey.

Finally, online marketplace bans are not confined to the more prominent cases of sport shoes and perfumes, see Figure 24. They pervade many more product categories and affect products that consumers frequently purchase.

**Figure 24 Spread of online marketplace bans in selected product categories, 2016**



Note: applies to e-tailers selling on online marketplaces.  
 Source: Copenhagen Economics based on Morar (2016) e-tailer survey.

### 2.3 Online marketplace bans harm SME e-tailers

Online marketplace bans harm many small e-tailers in many ways. The most immediate effect of online marketplace bans lies in decreased sales revenue for e-tailers selling on online marketplaces. Beyond this, SME e-tailers' long-term customer relations and profitability are put at risk when online marketplace bans are imposed.

In the previous chapter, we have reported the experience of two small business founders in the areas of fashion (footwear) and electronics, who experience the negative effects of

being on the receiving end of an online marketplace ban. The same experience is confirmed by the following two additional small business founders operating in the area of sports goods retail.

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### **Box 8 Niche business affected by online marketplace bans**

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**Christian Schläfer, FanSport24, Germany**

Online marketplace bans pose a substantial threat to the existence of small businesses like Christian Schläfer's FansSport24 and lead to a significant decline in revenues.

In 1999, FanShop24 was founded as the first online shop for sport fans and has been supplying licensed sport goods from Adidas and Nike such as jerseys and shoes to fans ever since. After Adidas imposed an online marketplace ban in 2013, the business nearly had to close down, its revenues declining by 80 per-cent. Even though this ban was eventually lifted, another ban was imposed by Nike in 2015 leading to a loss in revenues up to €75'000.

Next to the immediate decline in revenues, online marketplace bans harm FanSport24 in two other ways that reduce long term profitability:

- customers migrate to other online shops as a consequence of these bans
- a reduction in the product portfolio results in an image problem as the promise to offer everything within its special niche can no longer be fulfilled

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Source: Copenhagen Economics based on e-tailer interview.

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### **Box 9 Bans limit SMEs' chances to be found by customers**

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**Sean Cayless, Sportsfactoryshop, UK**

Online market bans limit the ability of small businesses to grow and to be found by customers says Sean Cayless, owner of a sporting attire business.

After beginning to sell online in 2007, Sean's business has experienced steady growth and to date he employs 20 people. His business was severely hit when brands including Nike and Oakley imposed online marketplace bans which resulted in lost sales of to at least £500'000. In addition, many customers were lost, impacting long-term profitability.

Sean explains that the power of online marketplaces is rooted in their ability to open up a much larger market, because without them small sellers can simply not be found by customers.

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Source: Copenhagen Economics based on e-tailer interview.

Is it possible to generalise from the experience of this diverse range of SME e-tailers? We have sought to confirm whether this anecdotal evidence is borne out in sales data across a variety of product categories and we find that indeed the effects reported by the small business founders is not just a personal experience but a wider phenomenon affecting retail patterns.

We have conducted an analysis of the development of e-tailers' sales value for a certain brand on the eBay marketplace before, during and after an online marketplace ban on

that brand and compared it to products in the same product category that, to our knowledge, were not affected by a ban during the same time period.

Many brands previously present on online marketplaces have imposed online marketplace bans. However, for most of these bans, there is no conclusive data on their duration, the time frame in which they were active and whether or not they were enforced by the brand owner. For a limited number of bans that have been subject to investigations and/or decisions by competition authorities or courts, we can define both a start and end-date and can be sure that the ban has been enforced towards retailers. We therefore focus on three selected online marketplace, see Table 3.

**Table 3 Case selection for GMV analysis**

Case	Country	Time frame	Product category	Start date*	End date*
Deuter	Germany	2013-2016	Outdoor equipment	1 March 2013	Active today
Ping	United Kingdom	2016	Golf equipment	Start 2015	November 2016 / August 2016
Adidas	Germany	2012-2015	Running shoes	1 January 2013	June 2014

Note: Start and end-dates were taken from relating competition authority/ court decisions; start dates are the coming into force of the ban within the selective distribution agreements of the brand owner; end dates are those of decisions to end the ban.

Source: Copenhagen Economics.

We conducted the analysis based on eBay data on Gross Merchandise Value (GMV) for different product categories. In our analysis, GMV describes the total sales revenue of merchandise (products) sold over a given time through an online marketplace by retailers present on that marketplace to consumers, i.e. B2C (business to consumer).<sup>32</sup> The GMV indicator provides information on a monthly basis on the total product sales revenue sold by retailers in a defined product category.

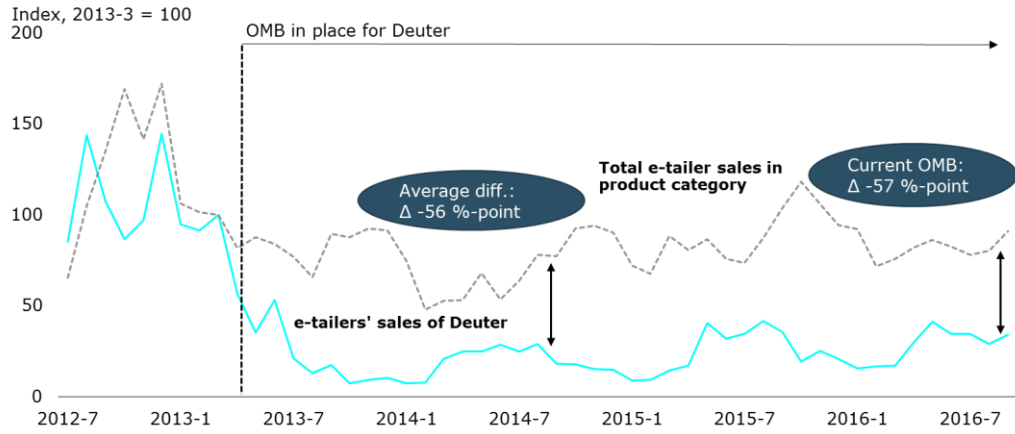
We find that, as expected, online marketplace bans affect immediately and significantly the sales of e-tailers of those brands on online marketplaces. Once the ban is lifted, it appears that, after a time lag, the ability of e-tailers to distribute their products via the marketplace is restored.

### **Deuter online marketplace ban**

Deuter, a German outdoor brand imposed an online marketplace ban starting in March 2013. The ban caused sales (GMV) of that brand on eBay to drop by 66 percent whereas the total outdoor category dropped by only 9 percent until today,

<sup>32</sup> GMV can also encompass consumer-to-consumer sales. We concentrate on B2C sales, i.e. sales by retailers on eBay that are registered as a business.

**Figure 25 Effect of Deuter online marketplace ban, Germany**



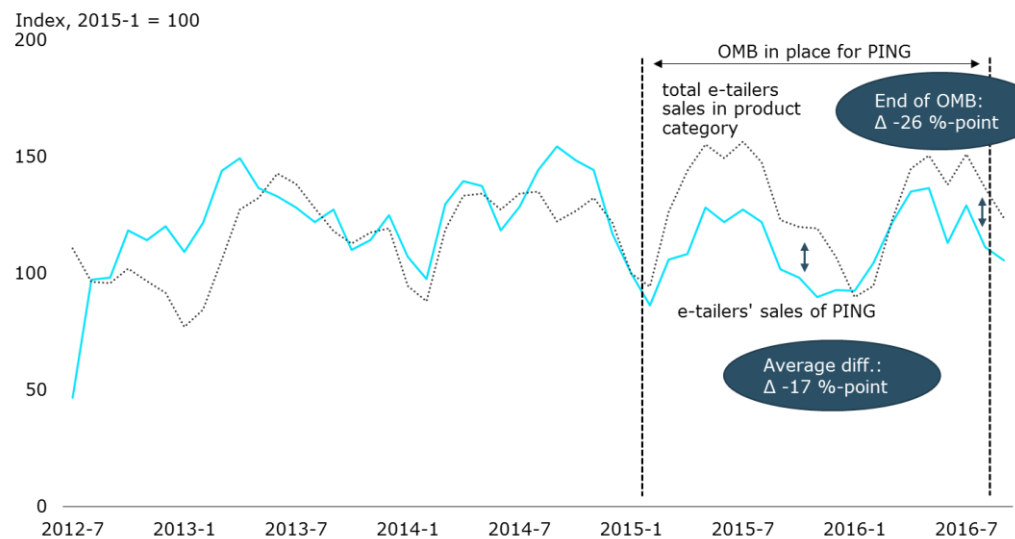
Note: OMB = Online marketplace ban.

Source: Copenhagen Economics analysis based on eBay.de data.

**PING online sales ban**

Over the period from January 2015 to August 2016, sellers of PING products were affected by an online sales ban (i.e. also a ban on sales on online marketplaces). As a result their sales grew only by 11 percent, whereas the total category grew by 37 percent.

**Figure 26 Effect of Ping online sales ban, UK**



Note: OMB = Online marketplace ban.

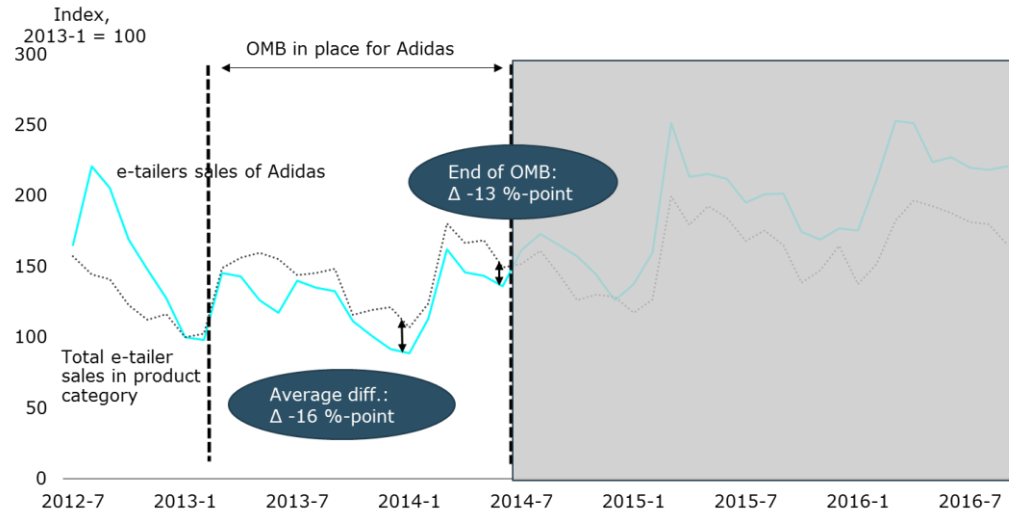
Source: Copenhagen Economics analysis based on eBay.de data.

**Adidas online marketplace ban**

Over the period from January 2013 to July 2014, sellers of Adidas shoes were affected by an online marketplaces ban.



**Figure 27 Effect of Adidas online marketplace ban, Germany**

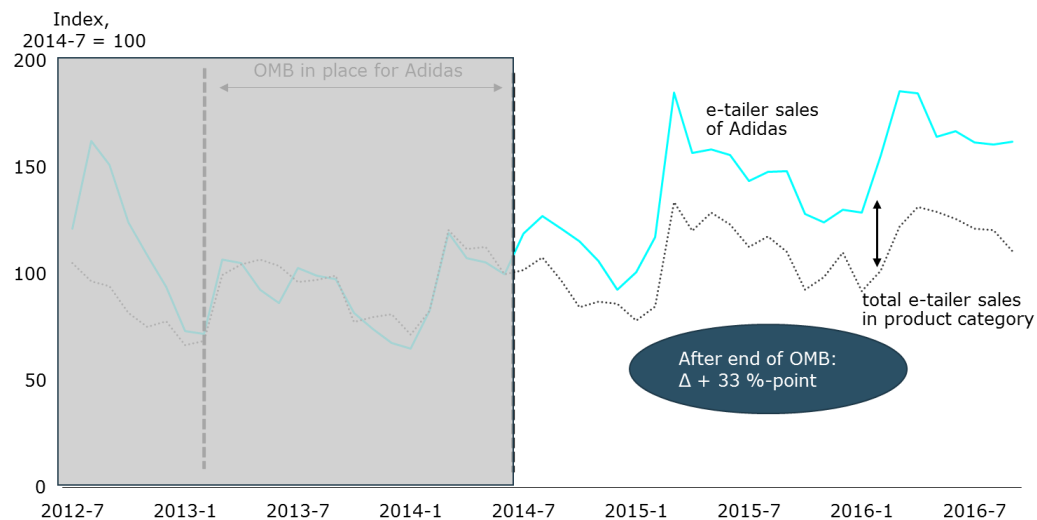


Note: OMB = Online marketplace ban.

Source: Copenhagen Economics analysis based on eBay.de data.

After July 2014, sellers of Adidas shoes were no longer affected by an online marketplace ban. Adidas growth potential was visibly restored.

**Figure 28 Adidas sales after end of online marketplace ban**



Note: OMB = Online marketplace ban.

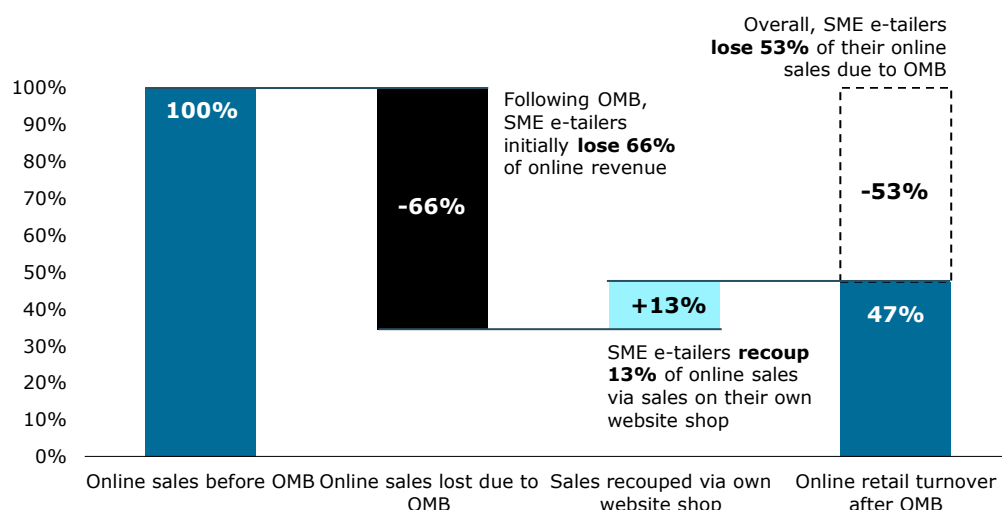
Source: Copenhagen Economics analysis based on eBay.de data.

### Effect of pervasive online marketplace bans

A Morar (2016) survey of e-tailers selling on online marketplaces asked retailers what share of their revenue they would lose if all brands imposed online marketplace bans. Retailers were also asked how much of the sales lost due to online marketplace bans they would be able to recoup by selling via other sales channels (e.g., their own website shop or their brick and mortar store).

Our analysis of the retailer responses shows that SME e-tailers initially stand to lose 66 percent of their total online sales revenue as a result of the online marketplace ban. In total, SME e-tailers estimate that they could only recoup 13 percent of their total online turnover by selling on their own website shop. This leaves an overall loss of 53 percent of online revenue due to an online marketplace ban, see Figure 29.

**Figure 29 SME e-tailers' sales loss from pervasive OMBs**



Note: Additional analysis (other retailer size categories; recoupment analysis) is presented in the Appendix to this report.

Source: Copenhagen Economics based on Morar (2016) e-tailer survey.

### Major upheaval as a result of online marketplace bans

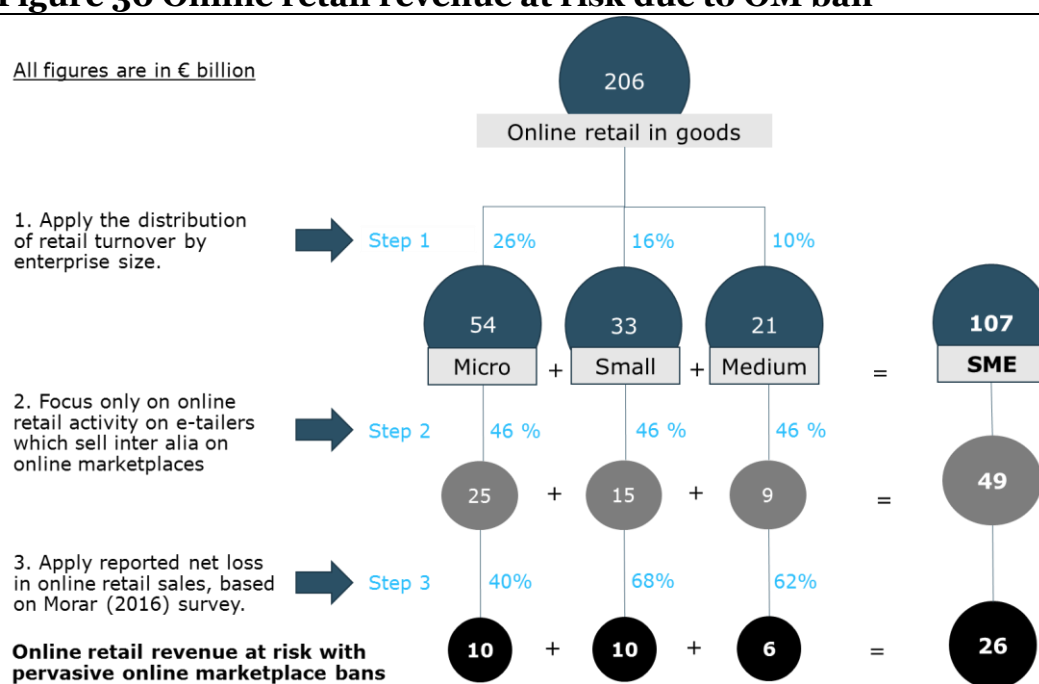
Unless EU institutions send a clear signal that online marketplace bans are not permissible under competition law, it is likely that brand owners will increase both the use and enforcement of online marketplace bans. Hence, a relevant question to ask is what part of online retail by SME e-tailers would be at risk in the scenario of a pervasive application of online marketplace bans.

The Morar (2016) survey collected empirical evidence on this, taking also into account the e-tailers' ability to recoup sales via channels not affected by online marketplace bans (i.e. own website store). Based on this recent data, as well as publicly available information on the size of online retail in Europe, we estimate the amount of online retail revenue at risk

in a scenario where online marketplace bans are pervasively applied. Specifically, we have estimated the impact on overall online retail revenues, thus not just the impact on the revenues transacted on online marketplaces.<sup>33</sup>

We find that for SMEs in the EU **€ 26 billion in online retail revenue** are at risk when online marketplace bans are imposed. This constitutes almost a quarter of all SME e-tailer online revenue.

**Figure 30 Online retail revenue at risk due to OM ban**



Note: Step 1 is based on Eurostat (distribution of retail enterprises, by turnover); Step 2 is based on Eurobarometer 439, p. 12; Step 3 is based on Morar (2016) e-tailer survey, Question 9 "If all brands imposed platform bans how much business would you lose in sales/revenue?", Question 10 "In the same situation with platform bans for all brands, what share of the sales/revenue lost would you be able to recoup by selling brands via other channels (e.g., your own website or brick and mortar retail)?".

Source: Copenhagen Economics estimates based on EC JRC (Duch-Brown and Martens) (2015), Eurobarometer (2016), Eurostat (2016), Morar (2016) e-tailer survey.

**Online marketplace bans affect the marketplace model thereby affecting SME retailers even more**

Online marketplace bans, when applied pervasively, undermine the key benefits that online marketplaces represent for SME retailers.

First, potential online retailers are less likely to enter the online retail market, if they cannot sell large parts of their product portfolio via online marketplaces. We have seen in Chapter 1 that starting up an online presence often happens on online marketplaces.

<sup>33</sup> The steps of our estimation and data sources are presented in detail in Appendix.

Second, for a large part of their products retailers will be deprived of the cost efficiencies online marketplaces provide them with. Online marketplace bans further limit e-tailers' possibilities to reach more and other consumers over the internet. For small and medium-sized "specialist" retailers that are known for their particularly high-quality distribution services, a ban on online marketplaces makes access to new customer groups difficult.

As reported by SMEs, maintaining an own online website store may not be sufficient to market products beyond the perimeter of their brick and mortar store. Even if many small retailers have their own online website store, they benefit largely from selling to consumers that find the retailer's products via online marketplaces.

Furthermore, foreclosing sales of branded goods on online marketplaces means foreclosing parts of mobile commerce for SME e-tailers.

Third, SMEs are deprived of the most efficient tools/-channel to engage in cross-border trade for a large share of their products. It is likely that, without the possibility to cheaply and easily sell cross-border via online marketplaces, SME e-tailer will decrease their cross-border sales activity.

This is demonstrated by the experience of small business founders, as shown below.

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### **Box 10 Bans affect his growing (cross-border) retail business**

**Monim Khiari, beautyfrench, France**

While working in the human resources industry, Monim began by sell on eBay to make some income on the side. By 2011 Monim had evolved his side project into a full time cosmetics business, thinking online marketplaces were the best channel to start online at low risk.

The business worked so well that he quickly moved from self-entrepreneurship to having a full-fledged company, now employing three people. Finding eBay the ideal platform for starting cross-border sales, at no additional cost except delivery, Monim quickly opened his listings for buyers around the world. Today his products reach consumers in 90 countries across Europe, the United States, Asia, Africa and Australia.

While selling on eBay also paved Monim's way to opening his own website shop, the online marketplace remains his first sales channel – especially for sales to consumers abroad.

Monim finds that online marketplace bans greatly affect his business. On marketplaces, one third of the brands apply bans to his business. In order to limit the risk of bans, Monim had to start tailoring his offers country-by-country.

He sees bans as a growing problem: in this year only, two new bans forced him to remove 35 over 300 products from his inventory, leading to a loss of 50 percent of turnover.

Source: Copenhagen Economics based on e-tailer interview.

Thus, we summarise the impact of online marketplace bans in the following table.

**Table 4 Impact of online marketplace bans on symbiosis between SMEs and online marketplaces**

<b>Symbiosis</b>	<b>Affected by online marketplace ban?</b>	<b>How?</b>
Get online	Yes	Entry barriers to online are higher
Grow online	Yes	Multi-channel retailing no longer possible
Be competitive online concerning cost, reach and innovation	Yes	Foreclosing part of mobile commerce
Overcome internal market frictions/ sell cross-border	Yes	Most efficient channel for cross-border sales largely disabled
Sell from remote locations	Yes	Most efficient channel for sales out of remote locations disabled

Note: See Chapter 1.4 for a description of the symbiosis.

Source: Copenhagen Economics.

## 2.4 Online marketplace bans harm consumer welfare

Online marketplace bans affect a large share of online shoppers. They reduce the welfare of these consumers by taking away the benefits that consumers enjoy when shopping on online marketplaces.

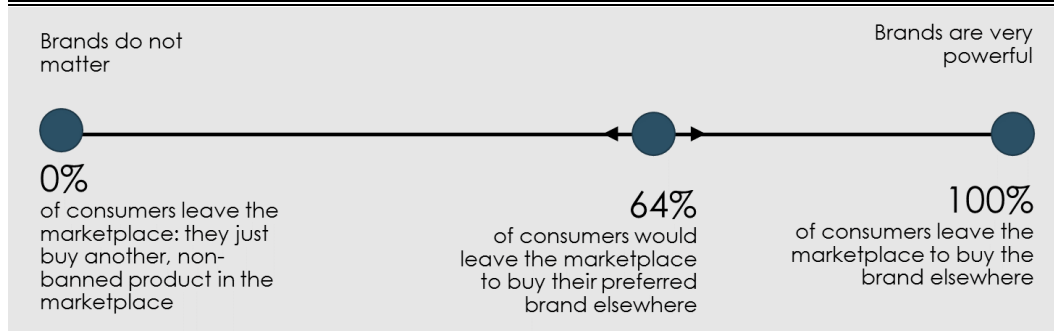
The strength of the effect of an online marketplace ban on consumers depends on the degree of diversion of consumers from online marketplaces, i.e. whether consumers will stay on the online marketplace or whether they need to switch to other sales channels. The degree of consumer diversion in turn depends on how powerful brands are:

- If brands do not matter greatly to consumers and they could no longer find the brand they are looking for on the marketplace, they would simply buy another brand on the marketplace. In this case, consumers are not diverted from the marketplace.
- If brands are extremely powerful, consumers would leave the marketplace in case they would no longer find their preferred brand on the marketplace. Consumers would then buy their preferred brand elsewhere. In this case, 100 percent of consumers would be diverted from buying on the marketplace.

We can gauge the power of brands to divert consumers from online marketplaces via empirical studies of stated preferences measuring how consumers would react to an online marketplace ban. According to Compass Lexecon (2016), 64 percent of consumers would leave the marketplace to buy their preferred brand elsewhere, if their preferred brand was subject to an online marketplace ban, see Figure 31.<sup>34</sup>

<sup>34</sup> This Compass Lexecon (2016) finding is based on an extensive, multi-country European survey, in the area of consumer electronics.

**Figure 31 Diversion of consumers from marketplaces**

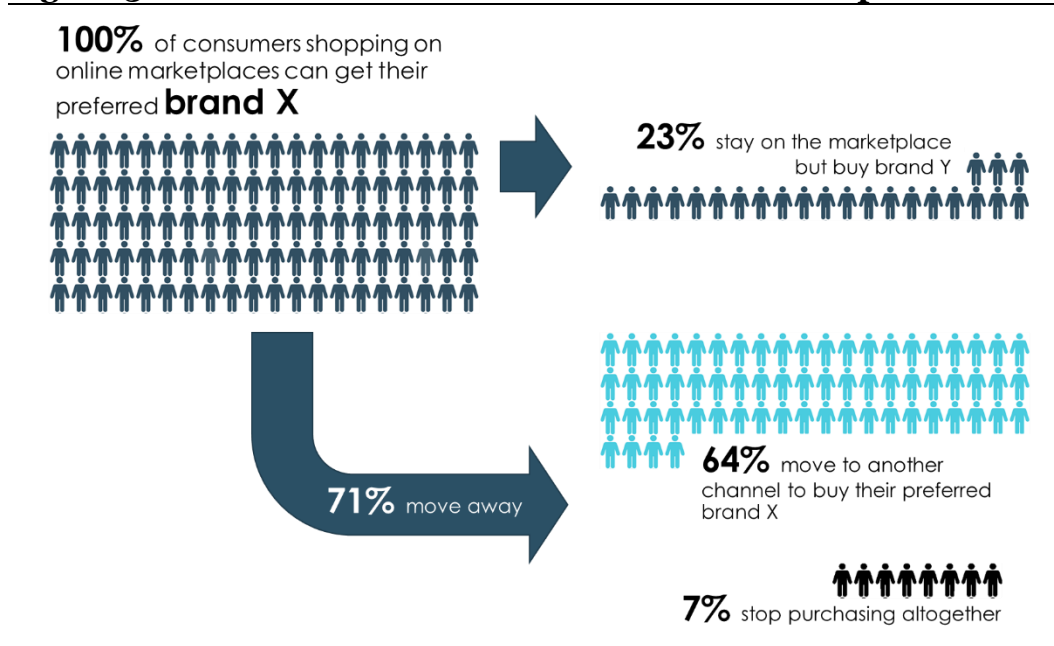


Source: Copenhagen Economics based on Compass Lexecon (2016).

Furthermore, online marketplace bans disrupt the consumer experience. Figure 32 shows a summary of stated consumer reactions to a situation where they can no longer find their brand X on an online marketplace. Of these consumers:

- Only 23 percent would stay on the online marketplace and resort to buying another brand Y. These consumers' welfare is reduced, if brand Y is not their preferred brand, but only their second choice.
- 64 percent of consumers move to another channel (brick&mortar or website store) to buy their preferred brand. These consumers' welfare is reduced because of increased search cost, decreased transparency and convenience, and decrease in time efficiency.
- 7 percent abandon the purchase altogether – leading to a deadweight loss.

**Figure 32 Consumer diversion due to online marketplace ban**



Source: Copenhagen Economics based on Compass Lexecon (2016).

In total, 71 percent of the consumers originally intending to shop via the online marketplace no longer buy on the marketplace – their purchases are diverted elsewhere or abandoned.

## 2.5 Online marketplace bans harm competition

According to competition economics, the overall effect of an online marketplace ban depends on three effects:

- **Effect on intra-brand competition** (i.e. competition among retailers distributing a certain brand)
- **Effect on inter-brand competition** (i.e. competition between brand owners of different branded products)
- **Effects on efficiency** in terms of maintaining a strong incentive for both retailers and brand owners to invest in the provision of sales-related services and brand-enhancing activities (e.g., brand presentation, advertisements)

In the following, we discuss these three effects from a competition economics perspective.

We find that online marketplace bans are, with certainty, detrimental to competition between retailers of the same brand (intra-brand competition). It is unlikely that competition between brands (inter-brand competition) is strong enough to outweigh the detriment of a restriction of intra-brand competition. Therefore, overall, online marketplace bans are likely to have an anti-competitive effect, which may result in an overall increase in prices faced by consumers.

### Insufficient efficiency gains from online marketplace bans

In order for online marketplace bans with anti-competitive effects to be allowed it needs to be shown that, on balance, consumers benefits and efficiencies flowing from the online marketplace ban outweigh the anti-competitive effects. This weighing of restrictions of competition against efficiency gains reflects the economic reasoning that, for certain brand products, selective distribution systems could be an effective way of increasing economic efficiency within a distribution chain.

In order for efficiency gains to be a valid counterweight to anti-competitive effects, three conditions should apply cumulatively:

- **Fair share for consumers:** it needs to be demonstrated that consumers get a fair share of these efficiency gains.
- **Indispensability of the restriction:** the online marketplace ban has to be indispensable to attaining the efficiency-enhancing effects.
- **No elimination of competition:** the online marketplace ban cannot substantially eliminate competition.

Since all of these conditions need to be fulfilled cumulatively, the standards for assessing the efficiency gains brought forth by the brand owner are high.

While the brand owner is free to set qualitative criteria for the distribution of products, we claim that a ban of sales via all online marketplaces amounts to the exclusion of an entire distribution channel. It has not been demonstrated that the online marketplace distribution channel, per se, holds possesses that would justify a generalized ban.

This view is supported by the German cartel office (Bundeskartellamt, BKA) which holds that there is no indication that an online marketplace ban creates per se any additional efficiency gains beyond the implementation of simple requirements for online sale. The BKA holds that brand image protection cannot be used by a brand owner as a general argument in order to justify additional restrictions to competition and that it is possible for brand owners to apply their quality criteria to online marketplaces.

*“Per se ban on sales via online marketplaces is not a qualitative criterion which is necessary to ensure the quality of the products concerned and the quality of their distribution. [...] In the present case there were no indications that the general functionality of open marketplaces, irrespective of their specific design, would necessitate a general ban on sales in order to safeguard the quality or distribution of the sports articles concerned. In any case, there is generally the less restrictive possibility of setting specific rules on how the contract products should be sold.”*

*“Online marketplace bans are also not appropriate to address free-rider problems: the problem exists irrespective of the distribution channel (online/ on OM) and occurs in both directions online and offline sales”*  
German Competition agency, remarks on Adidas’ online marketplace ban<sup>35</sup>

### **Online marketplace bans restrict competition between retailers of the same brand**

As detailed above, selective distribution agreements and, online marketplace bans specifically, restrict competition between retailers of the same brand, i.e. **intra-brand competition**. Competition between brands is restricted for two reasons.

First, by eliminating online marketplaces as the most transparent retail channel for their brand, brand owners raise consumers’ search costs. It is more difficult for consumers to compare price offers for one brand between several online website shops of retailers and brick and mortar stores than to compare prices of retailers on online marketplaces. If consumers are less able to compare prices, this dampens competition between retailers of the same brand.

Second, online marketplace bans limit retailers’ possibilities to reach more and other customers over the internet.

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<sup>35</sup> Bundeskartellamt (2014), p. 3; 6.



In fact, brand owners have a clear incentive to restrict intra-brand competition through online marketplace bans if they sell their products in their own retail stores (i.e. are vertically integrated). Recently, many brands have organized their own retail in brick and mortar stores and on their own website.

An online marketplace ban limits the number of retail competitors brand owners face on retail level. Limited price competition in turn leads to an increase in prices for the units the brand owner already sells. Moreover, the online marketplace ban yields additional retail sales for the brand owner, if consumers that previously bought the brand on online marketplaces are, after the ban, induced to buy from the brand owner's retail shop instead.

At the same time the brand owner might lose some volumes previously sold on online marketplaces to other, competing brands who do not impose an online marketplace ban. This is called inter-brand competition, i.e. competition between brands.

Whatever the balance from the brand owner point of view, our focus is the viewpoint of consumer, competition and social welfare.

### **Online marketplace bans restrict competition between retailers across different brands**

Restrictions of intra-brand competition are *only* seen as less problematic when well-functioning **inter-brand competition**, e.g., competition between different sport article brands, is present.

A key starting point is that it has not been demonstrated that inter-brand competition is a sufficient constraint with online marketplace bans.

Moreover, even the possibility of inter-brand competition does not make welfare concerns about online marketplace bans disappear, since in the previous section we have identified reasons why there can be social welfare detriment arising from online marketplace bans.

Competition between brands might be insufficient to outweigh the reduced competition between retailers of a single brand for two reasons.

First, for certain product categories, inter-brand competition is weak due to high market concentration. This has been confirmed by the German competition authority in the Adidas case.

*“Different sports article markets have a relatively high concentration of suppliers. Restrictions of competition in the distribution of a certain sports article brand can therefore have relative price effects which also weaken competition for other brands.”<sup>36</sup>*

Second, inter-brand competition is likely to have an insufficient effect. There are three reasons for this:

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<sup>36</sup> Bundeskartellamt (2014), p. 4.

1. Elimination of the most competitive retail channel softens inter-brand competition

In the presence of online marketplace bans, inter-brand competition is limited to competition *between* channels while inter-brand competition on online marketplaces themselves is reduced. Yet, it is on the online marketplace where price competition between brands tends to be most intensive. Hence, a marketplace ban eliminates the channel where inter-brand competition is strongest and therefore softens inter-brand competition.

2. Unilateral imposition of bans by brand owners shows that bans pay off

Brand owners would not have an incentive to unilaterally impose online marketplace bans, if inter-brand competition was strong, since they would simply lose sales volumes. Even if brand owners were unsure about the final effect of an online marketplace ban, they still might be tempted to experiment with it, leading to losses in social welfare and consumer welfare impact.

3. Decrease in intra-brand competition might lead to a decrease in inter-brand competition

Reduced downstream competition will lead to lower pass-through rates (wholesale price decreases will not be passed through to consumer, but absorbed by retailers), limiting the demand-stimulating effects of wholesale price decreases. This decreases a brand owner's incentive to decrease wholesale prices and, in turn, leads to higher retail prices.

Finally, even if inter-brand competition were to vibrant, consumer welfare would be reduced, because shopping for brands involves different channels and thereby increases consumers' search costs.

## 2.6 Concluding remarks and open policy questions

Based on the analysis in this chapter, we come to the following conclusions:

Online marketplace bans are today a widespread and rising practice that affect e-tailers of all sizes, in many EU countries and across many product categories to a similar, strong extent. Online marketplace bans by definition disable a retail sales channel that has become important for both SME e-tailers and consumers.

### **Harm to SME e-tailers**

Online marketplace bans harm many small e-tailers in many ways. The most immediate effect of online marketplace bans lies in a decreased sales revenue for e-tailers selling on online marketplaces. SME e-tailers indicate that they stand to lose 53 percent of their total online revenue from pervasive online marketplace bans. This is supported by analysis of e-tailer sales revenue on the eBay online marketplace. Beyond this, SME e-tailers' long-term customer relations and profitability are put at risk when online marketplace bans are imposed.

Moreover, online marketplace bans, when applied pervasively, undermine the key benefits that online marketplaces present to SME e-tailers, such as starting up and getting online as well as benefiting from the booming m-commerce. Online marketplace bans are likely to counteract the cross-border sales development that SME e-tailers have achieved thanks to online marketplaces. Consequently, such bans impair the EU policy aim of a frictionless, ever more deeply integrated Digital Single Market – particularly for SMEs.

### **Harm to consumers**

Online marketplace bans impact consumer welfare by taking away the convenience-enhancing features that online marketplaces present to consumers concerning the ease of search, transparency and time efficiency of the purchase.

### **Harm to competition**

We find that online marketplace bans lead to a restriction of competition between retailers of the same brand (intra-brand competition) that may not be sufficiently outweighed by competition between brands (inter-brand competition) nor by the unsupported efficiency gains arising from bans.

### **€ 26 billion at risk for SME e-tailers**

Unless EU institutions send a clear signal that online marketplace bans are not permissible, this would likely lead to an increased use and enforcement of these bans by brand owners. As a result, in a scenario where online marketplace bans become pervasive, this would result in a strong impediment to SME e-tailers. This would cause a major upheaval in retail commerce, depriving e-tailers of an estimated €26bn of online retail sales, diverted elsewhere.

As presented in this report, SME e-tailers benefit from the synergy with online marketplaces, while they seek to serve the evolving needs of European consumers. The SMEs' model to leverage online marketplaces for establishing and growing a multi-channel presence comparable to that of large firms is a successful model with strong potential yet to be tapped into. This is in particular because of the reduced barriers to cross-border retail trade for SMEs when they leverage online marketplaces. The existence of this model, now well proven and established, is great news for the European Digital Single Market.

Today, several online marketplace bans have been imposed, thus restricting SME e-tailers' ability to grow their business and serve consumers. The retail sector has evolved significantly over the past decade, reducing the extent of the benefits associated with online

marketplace bans – while leaving their known restrictive effect unchanged or more significant.

Moreover, by restricting SME e-tailers' ability to reach consumers on the online channels where consumers preferences are increasingly evolving to (e.g. mobile commerce, app-based e-commerce), these bans are likely to harm consumers by forcing a sub-optimal retail experience, compared to the consumers' desired retail channel and brand preferences.

Based on the evidence reviewed and presented in this study, European institutions should conclude that on balance there are no benefits per se from online marketplace bans. It should thus follow that the burden of proof for introducing and maintaining online marketplace bans should fall, case-by-case, upon the brand owner introducing these retail restrictions. This step would be helpful to clarify and resolve the legal grey area surrounding online marketplace bans.

Finally, this legal grey area seems at odds with the flagship EU policy of achieving a fuller, deeper Digital Single Market. Indeed, EU policymakers strive to promote the digital transformation of the European economy. It appears highly inconsistent with these policy objectives that one of the top EU sectors of economic activity – the retail sector – is discouraged from going online in an efficient way, due to the effects of online marketplace bans.

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## Appendix A

# Online retail sales loss from online marketplace ban

Here below we present further results and robustness checks concerning the estimations on online retail sales at risk under online marketplace bans.

## A.1 The Morar (2016) survey of e-tailers

The Morar survey of e-tailers was commissioned by eBay and conducted in October 2016. The survey covered 2,600 respondents across the UK, France, Spain, Italy and Germany. All respondents earn over US\$10,000 per year though selling via a range online marketplaces (whether eBay or other marketplaces). Alongside online marketplaces, respondents also sell via other retail channels such as own website or brick&mortar store.

Morar controlled for e-tailers' size (in terms of turnover. On that basis, we are able to infer the characteristics of each of the following enterprise classes, consistent with the European Commission Recommendation – the definition of micro, small and medium-sized enterprises<sup>37</sup>:

- Micro: turnover up to and equal to €2 million
- Small: turnover between €2 million and €10 million
- Medium: turnover between €10 million and € 50 million

When computing figures for aggregate of SME e-tailers from the figures reported for micro, small and medium-sized retailers by Morar, we have weighted them according to the distribution obtained from retail turnover by enterprise size reported by Eurostat (structural business statistics) for the year 2013. This allow us to calculate an SME-focused measure of the impact of online marketplace bans.

## A.2 E-tailers' loss due to pervasive online marketplace bans

The graphs below present the loss due to pervasive online marketplace bans perceived by e-tailers from different sizes. In addition to the graph presented in Chapter 2 of the main report, we also report recoupment in brick and mortar stores.

The results are based on the following questions in the Morar (2016) survey:

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<sup>37</sup> Available at <http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=URISERV%3An26026>.

Question: *If all brands imposed platform bans how much business would you lose in sales/revenue?*

Possible answers: 0-10%, 11-20%, 21-30%, 31-40%, 41-50%, 51-60%, 61-70, 71-80%, 81-90%, 91-100%.

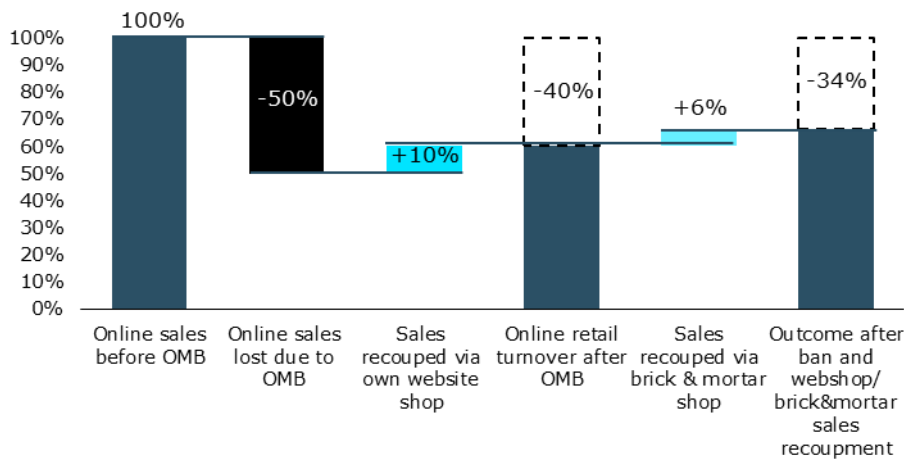
Question: *In the same situation with platform bans for all brands, what share of the sales/revenue lost would you be able to recoup by selling brands via other channels (e.g., your own website or brick and mortar retail)?*

Possible answers: 0-10%, 11-20%, 21-30%, 31-40%, 41-50%, 51-60%, 61-70, 71-80%, 81-90%, 91-100%.

Based on the answers to those two questions, we calculate the share of recoupment (both recoupment via the e-tailer’s own website store and brick and mortar). In the absence of specific information of these two recoupment channels, we make the conservative assumption that for these e-tailers recoupment follows the general distribution of online vs. brick and mortar retail sales reported by the respondents. This is a conservative approach (since logically the balance of online vs brick&mortar retail turnover can likely tilt towards the brick&mortar after an online marketplace ban) and will likely overestimate recoupment via the own website store. This has the effect of overestimate the amount of respondents’ online retail sales after the online marketplace ban, thus under-estimating our key result, that is the loss of online retail turnover.

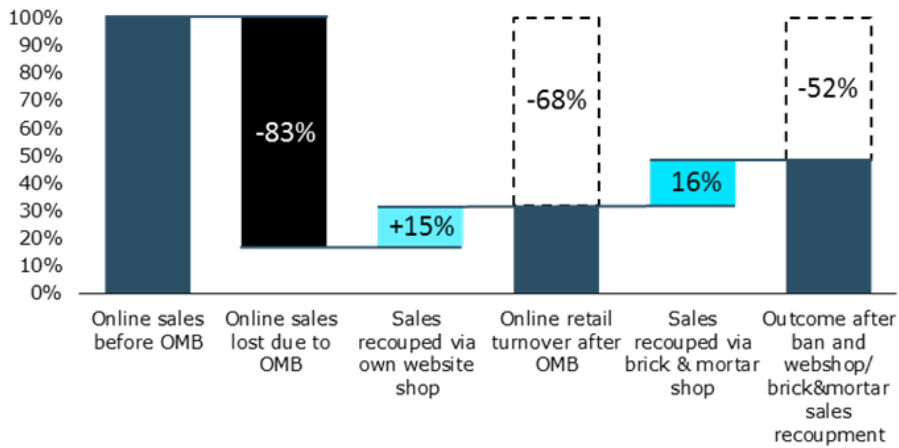
The following chart report, for each enterprise class – and then in aggregate for SMEs, the

**Figure A.1 Micro e-tailers’ retail sales loss due to online marketplace bans**



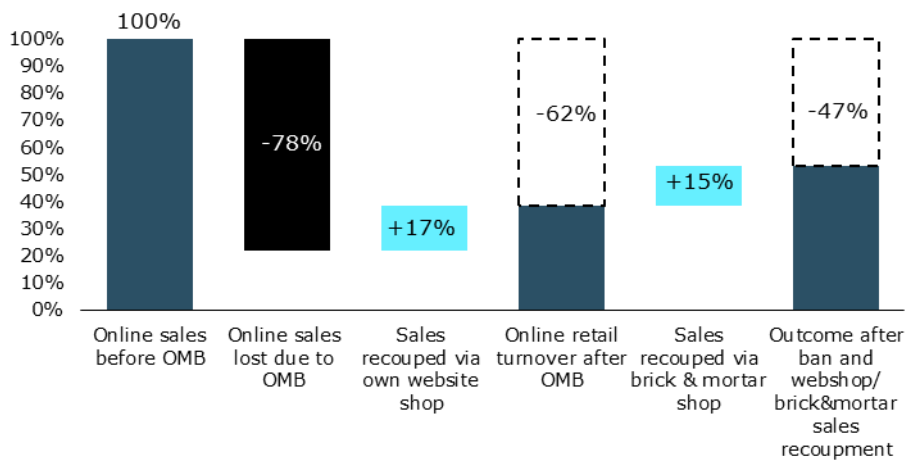
Source: Copenhagen Economics based on Morar (2016) e-tailer survey.

**Figure A.2 Small e-tailers' retail sales loss due to online marketplace bans**



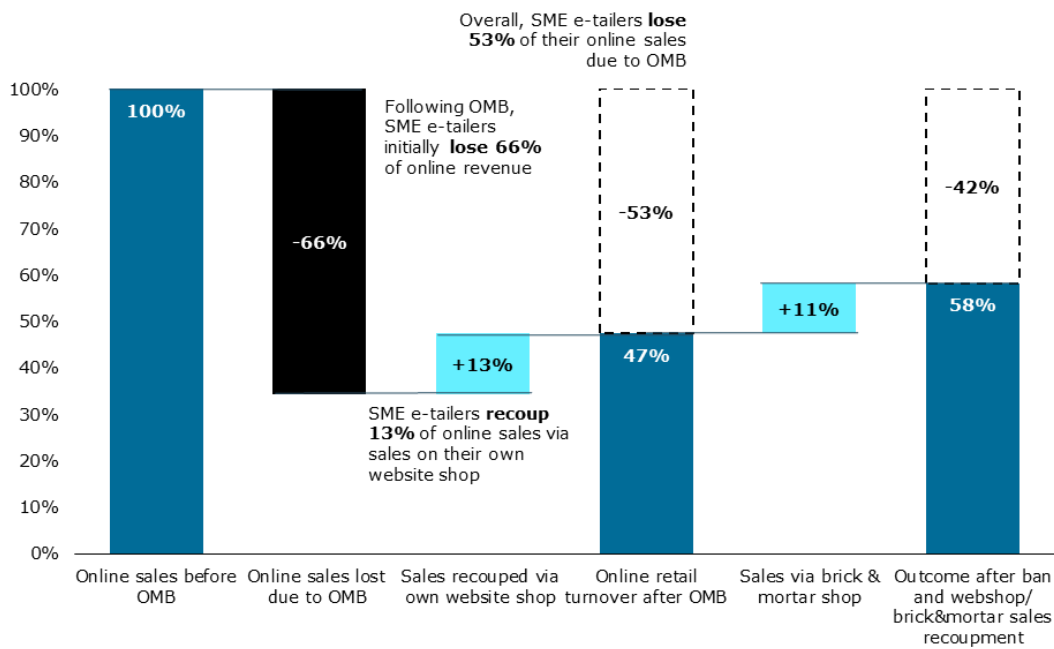
Source: Copenhagen Economics based on Morar (2016) e-tailer survey.

**Figure A.3 Medium e-tailers' retail sales loss due to online marketplace bans**



Source: Copenhagen Economics based on Morar (2016) e-tailer survey.

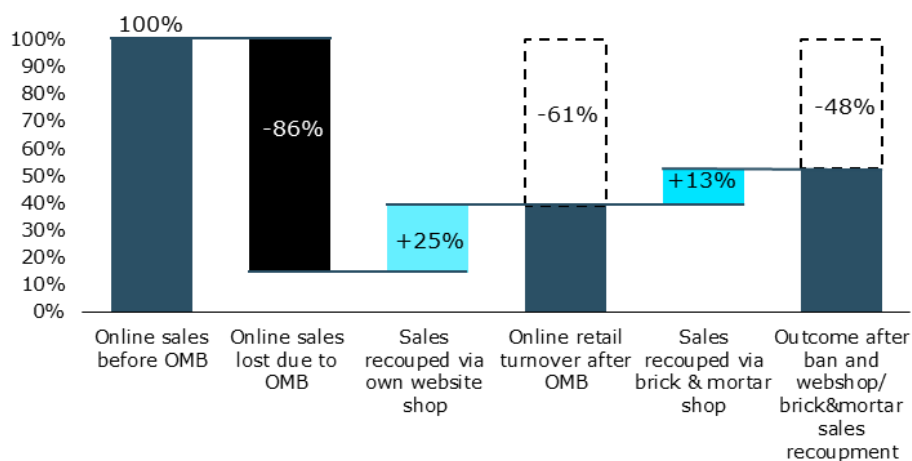
**Figure A.4 SME e-tailers' sales loss from pervasive OMBs**



Source: Copenhagen Economics based on Morar (2016) e-tailer survey.

In addition, some of the Morar (2016) survey respondents belonged to the class of large enterprises; however the survey class size was tapered off, thus making the responses for large enterprises not necessarily representative of the entire class. With this caveat, and in the interest of completeness, we display below the results of the retail sales loss analysis for this class, based on the same approach detailed above.

**Figure A.5 Large e-tailers' retail sales loss due to online marketplace bans**



Source: Copenhagen Economics based on Morar (2016) e-tailer survey.

### A.3 Online retail revenue at risk due to online marketplace bans

#### Step-by-step explanation of estimation procedure

We estimate the online sales revenue at risk for SME e-tailers in the following manner, see Figure below. We take as starting point the estimates by the EC JRC, which set the value of online retail turnover in the EU in the year 2014 at of € 206 billion.<sup>38</sup> This is a measure of online retail, that is e-commerce of merchandise, i.e. goods. We then apply the following three steps:

1. From this estimate, we derive the online turnover generated by micro-, small and medium-sized e-tailers by applying a distribution obtained from Eurostat. The Eurostat data is retail turnover by enterprise size (structural business statistics) for the latest available year (2013 - micro: 26%, small: 16%, medium: 10%). It is a measure reflecting the distribution of all retail activity (both online and offline). The result is an estimate of online retail sales by SMEs of €107 billion. (see Step 1 in the figure below)
2. Online marketplace bans only directly affect the revenue of e-tailers that sell (at least a part of their products) on online marketplaces. The Morar (2016) survey sample covers e-tailers selling inter alia on online marketplaces, i.e. both e-tailers

<sup>38</sup> European Commission Joint Reserach Centre – Duch Brown and Martens (2015), p. 7.

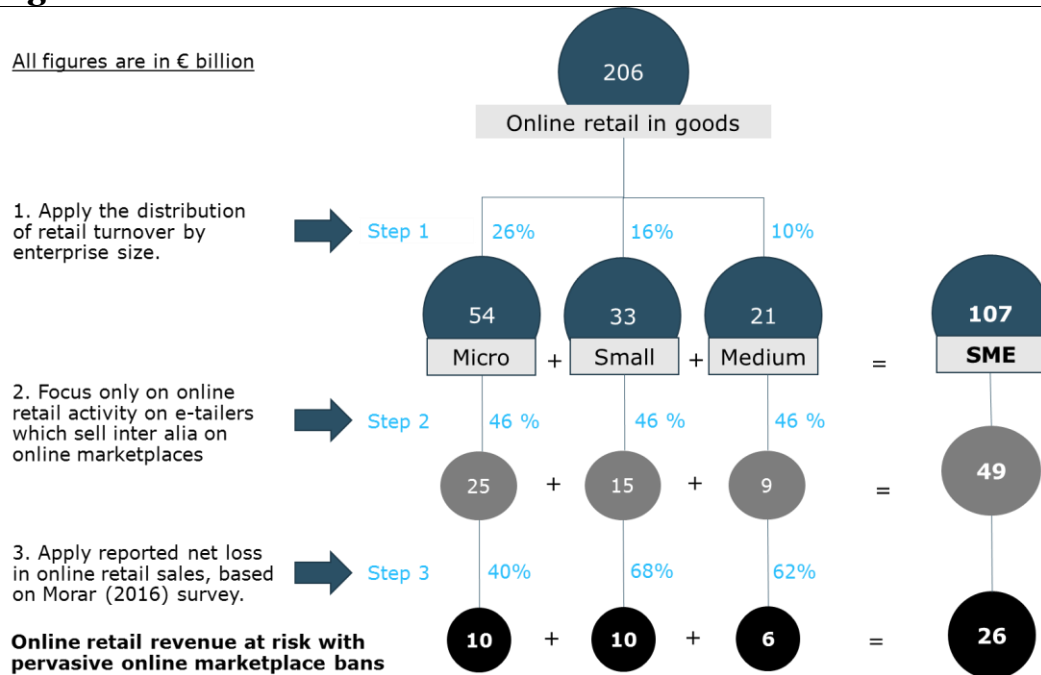
that sell on online marketplaces and via their own website shop and e-tailers' that only sell via online marketplaces. Thus we cannot apply directly the statistics in the Morar (2016) survey to the entire online retail turnover reported in the EC JRC (2015) estimate. This is because the entire online retail turnover includes the economic activity of those firms that do not currently rely on online marketplaces to sell goods online. In order not to overestimate impact we must therefore first of all control for this activity. We do so we rely on the EC Flash Eurobarometer (2016) data, which reports a suitable proxy, i.e. the distribution of firms by their current choice of online sales channel (e.g. own website store vs online marketplace).<sup>39</sup> Based on this source, we estimate that 46% of SMEs' online retail is activity of firms that use, inter alia, online marketplaces to sell online, thus estimated at €49 billion. It is only within this subset of activity that we apply the statistics in the Morar (2016) survey, to ensure a like-for-like approach (see Step 2 in the figure below)

3. We calculate the EU-wide total online retail net loss based on the results of the Morar (2016) survey, for each enterprise class. The total net loss figure describes the total share of online revenue lost minus the share of the revenue recouped online (based on the analysis of the Morar survey, as detailed above). This leads us to estimate a EU-wide value of SME online retail revenue loss of €26 billion (see Step 3 in the figure below).

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<sup>39</sup> European Commission (2016), Flash Eurobarometer 439 Report on the use of online marketplaces and search engines by SMEs, p. 12.

**Figure A.6 Online retail revenue at risk due to OM ban**



Note: Step 1 is based on Eurostat (distribution of retail enterprises, by turnover); Step 2 is based on Eurobarometer 439, p. 12; Step 3 is based on Morar (2016) e-tailer survey, Question 9 "If all brands imposed platform bans how much business would you lose in sales/revenue?", Question 10 "In the same situation with platform bans for all brands, what share of the sales/revenue lost would you be able to recoup by selling brands via other channels (e.g., your own website or brick and mortar re-tail)".

Source: Copenhagen Economics estimates based on EC JRC (Duch-Brown and Martens) (2015), Eurobarometer (2016), Eurostat (2016), Morar (2016) e-tailer survey.

**Robustness check of online retail revenue figure**

The calculations detailed above take as starting point the estimate for EU-wide online retail turnover from the EC JCR (Duch Brown and Martens 2015, p. 7), amounting to €206 billion.

## Figure A.7 Online retail turnover in the EU

**Table 1: Evolution of the volume of the retail sector in the EU-28 and its components, 2000-2014 (Bln euros)**

	2000	2005	2010	2014
Total	2,829.4	2,938.2	2,923.6	2,849.2
Online	13.0	50.5	118.6	206.0
Of which:				
Pure Internet retailers		15.9	44.1	80.2
Mobile			3.4*	27.8

\* Data refers to 2011.  
Source: Euromonitor.

Source: EC JCR (Duch Brown and Martens, 2015), p. 7

As a robustness check, we compare this figure with an alternative – more indirect – estimate approach. We do so, by taking as starting point the Eurostat results in a generalist survey of enterprises. This survey reports what share of enterprise-wide turnover is due to “B2C web sales” (thus both sale of goods and of services) in 2013. According to Eurostat, across all SMEs this share is of 1% (with no decimal reported). Given the overall SME turnover, this leads to an estimate for SME B2C web sales of €144bn, encompassing both the retailing of goods and of services.

## Table A.1 Estimate of B2C web sales

	In € billion	In %
Total turnover, SMEs (2013)	14,416	
Share of total SME turnover corresponding to B2C web sales (2013)	144*	1%
Total turnover, Large enterprises (2013)	11,540	
Share of total large enterprise turnover corresponding to B2C web sales (2013)	230*	2%
Total turnover of B2C web sales	<b>374*</b>	

Note: \*Copenhagen Economics calculations based on Eurostat (Value of e-commerce sales) figures.

Source: Copenhagen Economics based on Eurostat.

As a second step, we apply the findings of E-commerce Europe (2015), which found that overall European e-commerce turnover includes 53% of sale of goods.<sup>40</sup> Applying this share leads to an estimate of €75bn for the EU-wide SME online retail turnover.

This indirect estimate (€75 billion) is 30% smaller than the value of €107 billion applied in our main estimate (see Split 2). As a result all the descendant calculation results are 30% smaller, if this alternative approach is adopted. This implies that the final result for the online retail revenue at risk with pervasive online marketplace bans is equivalently estimated as 30% lower, i.e. at €18 billion.

While €18 billion is a sizable amount (and broadly in the same ballpark as our main estimate of €24 billion), we consider that this figure is likely to an underestimate, since the E-

<sup>40</sup> E-commerce Europe (2014).



commerce Europe goods/service e-commerce turnover split is not a statistics specific to SMEs. This split is the composition of the (unknown) goods/service split for SMEs and for large enterprises (also unknown). When considering that E-commerce services in the area of travel tickets, music/video/editorial content is predominantly the domain of large enterprises, this suggests that the situation would be reversed for goods.<sup>41</sup> In conclusion, this robustness check confirms the broad validity of the main estimates presented in the report.

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<sup>41</sup> This direction of bias is confirmed when comparing the result of the Eurostat survey, focused on “B2C web sales” (thus both goods and services). On this basis, while the turnover estimated for SMEs is €144 billion, the figure for large enterprises is of €230 billion. This would imply that SMEs are responsible for 39% of e-commerce turnover, when we look at both e-commerce of goods and services – consistent with a preponderance of large firms in the domain of e-commerce of services.

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Copenhagen Economics is the leading economic consultancy in the Nordic region. Our economists provide advice and analyses in the fields of competition, regulation, international trade and impact assessment.

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IP Valuation



Postal & Delivery



Finance & Tax



Trade & Internal Market



Transport

We provide hard facts and clear stories, enabling our clients and their stakeholders to make superior decisions based on sound analysis.

We advise companies, authorities and policy makers when market meets regulation and conflicts arise. We help our private sector clients handle conflict cases and guide them on how to prosper through regulatory management. We help our public sector clients evaluate and devise new regulation.

Founded in 2000, the firm

- Is partner-owned
- counts more than 70 employees, mostly with Ph.D. or M.Sc. in Economics
- includes Economists from various nationalities / languages (among which British, Danish, Dutch, Finnish, French, German, Italian, Lithuanian, Norwegian, Swedish)
- and operates across the world.

Global Competition Review (CGR) lists Copenhagen Economics as one of the top 20 economic consultancies in the world.