

1. I will submit that the New Zealand Commerce Commission (the Commission) should decline the application to merge by Foodstuffs North Island and Foodstuffs South Island (the Co-ops), and should take further steps to achieve greater competition in the retail grocery market in the long-term interests of NZ consumers.
2. In terms of the Commission's *Statement of Unresolved Issues*, I share the concerns that 'the Proposed Merger would substantially lessen competition due to unilateral effects in relevant upstream markets for the acquisition of groceries' (*Statement*, at 9.1).
3. However, I will not attempt to substantiate my concerns with the buying side of the grocery market in this Submission.
4. My Submission will focus on unilateral effects on competition in the downstream (retail) market for groceries and other products supplied by supermarkets in NZ – effects not considered by the Commission to be an unresolved issue.¹
5. Specifically, I submit first:

HAZLEDINE SUBMISSION I: The proposed Foodstuffs merger would generate a substantial lessening of competition in the retail market because it would foreclose future competition generated by the two Co-ops entering each other's markets to compete independently. The request to merge should therefore be refused.

6. At present, the two Co-ops compete each with Woolworths but not with each other, because they each choose to supply groceries at retail in only one market -- North Island or South Island. That is, in terms of the dominant players, the NZ retail grocery industry operates as two distinct regional duopolies.
7. However, there is no technical or economic reason for them to not compete across the country, such that the NZ retail grocery industry could then operate as a single, national triopoly of independent competitors.
8. The Commission has already determined that an increase in the number of independent large grocery chains across the NZ marketplace would significantly enhance the long-term interests of NZ consumers.²

¹ The Commission does see problems with the possibility of the merger affecting the likelihood of coordinated effects on pricing, between the Co-ops and Woolworths.

² For example, the Commission's *Market Study into the Retail Grocery Sector: Final Report* (8 March, 2022), lists (paragraph 9.22) the likely benefits of 'entry or expansion' in terms of improvements in: prices, consumer

9. I note that the corresponding significant lessening of competition likely as a result of approval of the proposed merger is loss of *potential* competition.
10. Loss of potential competition is not dealt with in the Commission's otherwise useful *Mergers and Acquisitions Guidelines* (May 2022). The issue is covered in the latest (2023) revision of the US Merger Guidelines in the exact same context of the NZ Foodstuffs merger application, as reported:

A merger between two firms that do not presently compete with one another can harm potential competition in two ways: It can eliminate the possibility of future competition after entry by one or both of them into a market in which the entrant did not previously compete, which the courts have called “actual potential competition”; and it can eliminate the present competitive pressure on firms that are already in the target market to reduce price or improve product quality in response to the threatened entry by one or both of the merging parties, which courts have called “perceived potential competition.”³

11. It is the first of these -- “actual potential competition” -- that is at risk in the present case.
12. I wish in this submission to examine further the reasons that we now have an industry structure that includes two bifurcated regional Co-ops operating under the Foodstuffs banner. The applicants’ continued claims that their merger would not reduce competition because they don’t currently compete with each other seems to assume that the status quo is some sort of immutable state of nature.
13. But it is not a state of nature. It is a strategy chosen by the Co-ops themselves. In an “OpEd” (Opinion) piece I wrote that was published by the media company Stuff on the website of *The Post* newspaper, and then reprinted on the University of Auckland website, I described the strategy of the two Co-ops as:

choice, innovation, productivity and efficiency. (‘Expansion’ means growth in existing small competitors’ market shares.)

³ R.J. Gilbert and A.D. Melamed, ‘Potential Competition and the 2023 Merger Guidelines’, *Review of Industrial Organization* (2024) 65:269-302

The cosiest of cosy agreements to not poach retail customers from each other.⁴

14. In a letter (attached to this Submission, as is the OpEd), the Co-ops' lawyers included this in a list of what they alleged are "defamatory statements".

15. In the Commission's *Statement of Unresolved Issues*, (published about a month after the lawyers' letter) we find:

[B]ased on the evidence before us, we do not consider that there are any arrangements between the Parties to not compete, or that prevent them from competing, in any retail grocery markets. (at para 64).

16. This statement is incorrect. There is an arrangement to not compete at retail, and the Commerce Commission is well aware of it.

17. The arrangement is helpfully highlighted in the Co-ops' own December 2023 *Application to the Commission for permission to merge*⁵, which brings forward a 2001 statement by the Commission in its consideration of the Woolworths/Progressive Enterprises merger. At that time there were two North Island Co-ops:

At the retail level, the three [Foodstuffs co-operatives] do not compete as they each operate in quite separate regions. Each Foodstuffs company holds the rights to the banner names in their respective areas. This precludes (say) Foodstuffs (Wellington) opening a Pak'N Save in Auckland.⁶

18. I expect that this clever device is sufficient to effect total regional separation of markets, since the individual Co-ops would have to invent new and different brand names to set up in markets outside their designated area. There may also be other formal and/or informal policies and practices serving to reinforce the separation.

⁴ Tim Hazledine, 'Foodstuffs wants to merge its co-ops, but consumers need the opposite', *The Post*, May 22, 2024. <https://www.thepost.co.nz/nz-news/350284911/foodstuffs-wants-merge-its-co-ops-consumers-need-opposite>, attached to this Submission

⁵ *Notice seeking clearance for the merger of Foodstuffs North Island Limited and Foodstuffs South Island Limited* PUBLIC VERSION 14 December 2023

⁶ Commerce Commission, *Progressive Enterprises Limited and Woolworths (NZ) Limited*, Decision No. 448, 14 December 2001, at paragraph 62

19. So, my claim that the Co-ops have an agreement to not poach retail customers from each other is not a defamatory allegation. It is a simple statement of fact.
20. This arrangement has been in place for many decades, in full view of the Commerce Commission and everyone else. I can find no explicit claim that the Commission has openly approved the arrangement. The closest I can get is the statement by the Co-ops in their application for clearance to merge (at para 113):

The Commission has considered the Foodstuffs co-operative structure on several occasions, and has acknowledged that the co-operatives do not compete in relation to the retail supply of groceries due to their different geographies
21. No information is offered on the nature of the ‘several occasions’ on which the Commission has ‘considered’ the matter. My COD gives as one possible meaning of the word ‘acknowledge’: “recognise the validity of”. This could be the sense intended in the Co-ops’ application.
22. In any case, it is reasonable to assume that the managers of the Co-ops have been acting all these years on the assumption that, if the Commission or other parties had concerns about the legality of the market-allocating agreement, they would have raised them by now. And they apparently haven’t, until now.
23. I certainly did not assert otherwise in my OpEd article, and the claim by the lawyers in their letter that I ‘imputed’ that Co-op management were knowingly engaged in “illegal, criminal and anti-competitive practices” is ridiculous (and possibly defamatory).
24. For clarity: the market allocating practice certainly is anti-competitive (a restrictive practice, under the Act), but that doesn’t mean it is illegal/criminal. Such practices may be legitimately undertaken within a business unit defined as a ‘person’ under the Commerce Act. To state the obvious: you cannot force a firm or other ‘person’ to compete with itself.
25. I expect that the real purpose of the letters sent to Stuff and the University of Auckland was to chill critical discussion of the proposed merger. This interpretation is consistent with the sentence in the letter to the university:

Provided these defamatory *[sic]* statements are removed *[from the University website]* by 5pm on 25 June 2024, this will resolve matters as far as Foodstuffs is concerned

26. If so, they partially succeeded. My university's officials caved in at once. So much for defending the 'critic and conscience' role of the academy! The media outlet *Business Desk* did not print any of the allegedly defamatory statements, "so as not to repeat the potential defamation".⁷ And I detect a cautious legalistic tinge to the Commerce Commission's statement reprinted above in paragraph 15.
27. However, most importantly, Stuff stayed staunch, and my piece can still be downloaded from *The Post* website, at <https://www.thepost.co.nz/nz-news/350284911/foodstuffs-wants-merge-its-co-ops-consumers-need-opposite>
28. It is my hope that the Commerce Commission will open up on its views with respect to the Co-ops' market allocating arrangements. There does seem to be a difficulty here. If the two co-ops are to be treated as separate 'persons' in the structural matter of a proposed merger, why then can they be considered as a single 'person' in the conduct matter of deploying restrictive practices?
29. So, my second Submission to the NZ Commerce Commission is:
- HAZLEDINE SUBMISSION II:*
- The NZCC should explain the reasons for its tacit approval in the past of the market allocating practices of the Foodstuffs Co-operatives, and consider revising its views in the light, in particular, of its 2022 findings (in its *Market Study into the retail grocery sector*) of significant market power currently exercised by the supermarket chains serving the sector.
30. The present arrangements of the Foodstuffs Co-operatives are already some distance along the road to them functioning as independent competitors. The Co-ops are, in effect, seeking permission to go backwards on this road; to full coordination of their activities. In my OpEd article I proposed that the Commission take the opportunity to push the Co-ops towards full independence, such that they would become entities competing with each other throughout New Zealand.
31. Other submitters may propose possibly more radical interventions, such as splitting the Pak'nSave and New World chains into separate businesses.
32. Our shared concerns are, likely, twofold: First, the evidence, most recently documented in the NZCC 2022 *Market Study*, of significant retail market power being exercised in the grocery sector; second, the apparent (from

⁷ Gregor Thompson, 'Foodstuffs North Island alleges defamation over merger opinion piece', *Business Desk*, 03 July, 2024.

experience of the past decades) unlikelihood of incumbents' market power being challenged by large-scale entry into the sector of a new competitor.

33. Accordingly, my third Submission to the NZ Commerce Commission is:

HAZLEDINE SUBMISSION III:

The NZCC should act, having if necessary first secured from government and/or the courts the authority to act, to split the Foodstuffs Co-operative into two or more fully independent competitors in the NZ grocer products market.

Respectfully submitted, August 12, 2024

Tim Hazledine is Emeritus Professor of Economics at the University of Auckland

Attachment: Hazledine article in *The Post*, May 22, 2024

The OECD --- the ‘rich nations’ club – is calling for action to increase competition in NZ’s grocery sector. In its *Economic Survey*, released on May 6, it states that two supermarket chains – Australian-owned Woolworths, and the New Zealand cooperative Foodstuffs -- dominate the market, setting prices and claiming profits that are high by international standards.

The OECD envisages that break-up of the ‘duopoly’ might eventually ‘prove warranted’, but warn that such action will be ‘intrusive and complex’. But what they and everybody else haven’t seemed to notice is that there is a simple pro-competition option just sitting there, and that this is triggered by the recent actions of one of the big players in the market

The cooperative is actually two independent legal entities: Foodstuffs North Island and Foodstuffs South Island. Each is owned by the franchise holders in their particular island, including New World, Pak’nSave and Four Square grocery stores. They compete throughout the country with Woolworths (formerly Countdown). But they don’t compete with each other – by longstanding arrangement, neither coop sells groceries at retail in the other’s territory.

The two co-ops have now approached the NZ Commerce Commission for authorisation to merge into a single entity: Foodstuffs NZ.

Their most prominent explicit motive for merging is so to coordinate their purchasing arrangements with grocery product manufacturers and suppliers. Currently, each of the two regional co-ops handles their own purchasing independently.

This turns out to be just about the only major commercial function they do carry out independently. As the NZCC’s *Statement of Issues* explains, the co-ops already coordinate their purchasing and marketing of private label products. Their two wholesaling businesses -- Gilmours in the North Island, Trents in the South -- operate as one in the national supply of groceries and services to institutions and other non-retail customers. And, above all, they have this, the cosiest of cosy agreements to not poach retail customers from each other.

All these arrangements are generally *per se* illegal under the Commerce Act, if implemented by otherwise independent competing firms. They are covered by prohibitions on price-fixing and market-sharing that can result in substantial fines and even prison terms if breached. Put it this way: if either co-op tried it on with Woolworths – well, the NZCC would be down on them like a ton of bricks.

This raises two questions: how have they gotten away with it? And, given that they have gotten away with it, why haven’t they just quietly gone ahead with similar arrangements for their purchasing activities, without seeking NZCC authorisation?

I don't know, but I wouldn't be surprised if the co-ops have become uneasy about the legal status of their existing anti-competitive practices, and have decided to try to trump the whole issue by applying to become a full-scale legal monopoly: thus safely internalising practices to be well out of the reach of competition law.

It really is an extraordinary situation. For years the Commerce Commission and others – including me, and, now, the OECD – have bemoaned the lack of a third competitor in the NZ supermarket sector. We've hoped for a 'white knight' – perhaps the German grocer Aldi – to wade in and ginger-up pricing etc in this sleepy sector. But it's never happened.

Yet, all along, there was a third competitor right there under our noses! We do have now three statutorily independent supermarket players – all that is required is to get them to act independently.

The overall case that pro-competitive action is needed has been made previously by the NZCC itself and others. It's not just about prices. NZ supermarkets are indeed sleepy. Yes, they are usually clean and well-lit. They are competent at stocking all the branded grocery products supplied to them by manufacturers. But they are generally lack-lustre at anything a bit bespoke --- cheeses, butchery, bakery, delicatessen, flowers. And their service standards wouldn't be acceptable elsewhere in the retail sector. As we all know from personal experience, it is quite possible to spend more time queuing to pay for your groceries than it took you to put them, unaided, into your trolley.

The NZ Commerce Commission should decline authorisation for the cooperatives' merger and go much further. Probably with the assistance of Parliament and the courts, the two Foodstuffs entities should be pushed to behave like normal competitors.

Ask for name changes: to Foodstuffs A and Foodstuffs Alpha, or perhaps something zingier. Instruct all three supermarket chains to continue to act totally independently in negotiating contracts with suppliers. Instruct the two co-ops to stop coordinating their private label businesses. Forbid them to continue colluding on their important wholesale grocery services. And – most important of all – pull down the invisible wall they have constructed to separate North and South Island grocery markets, which, in particular will require giving individual holders of a supermarket franchise the right to switch to a different co-op. That'd be a good start.

Attachment: lawyers' letter



21 June 2024

Kiri Coughlan
Director, Communications and Engagement
University of Auckland
Auckland

By email

Dear Kiri

DEFAMATORY ARTICLE ON THE UNIVERSITY'S WEBSITE

- 1 We act for Foodstuffs North Island Limited (**Foodstuffs**).
- 2 Foodstuffs has recently learned that Emeritus Professor Tim Hazledine has published an article titled "Foodstuffs wants to merge its co-ops, but consumers need the opposite" (the **Article**) on the University of Auckland's website. The Article can be accessed at this [link](#).
- 3 This Article appears to reproduce the article Professor Hazledine authored with the same title published by The Post on 22 May 2024.
- 4 We have already written to The Post and Stuff regarding the defamation in the original article, and now write to you to identify the same in this Article.
- 5 The Article contains several defamatory statements, including:

"And, above all, they [Foodstuffs North Island and South Island] have this, the cosiest of cosy agreements to not poach retail customers from each other."

"All these arrangements are generally per se illegal under the Commerce Act if implemented by otherwise independent competing firms. They are covered by prohibitions on price-fixing and market-sharing that can result in substantial fines and even prison terms if breached. Put it this way: if either co-op tried it on with Woolworths – well, the Commerce Commission would be down on them like a ton of bricks."

"This raises two questions: how have they gotten away with it? ... I don't know, but I wouldn't be surprised if the co-ops have become uneasy about the legal status of their existing anti-competitive practices and have decided to try to trump the whole issue by applying to become a full-scale, legal monopoly, thus safely internalising practices to be well out of the reach of competition law."

"Probably with the assistance of Parliament and the courts, the two Foodstuffs entities should be pushed to behave like normal competitors."

- 6 These statements convey a number of defamatory imputations, including that:

- 6.1 Foodstuffs is currently engaged in illegal, criminal and anti-competitive practices and has entered into an anti-competitive agreement; and

- 6.2 There are reasonable grounds to suspect that the owners or operators of Foodstuffs know that they are acting illegally and anti-competitively.

- 7 There are no defences to these imputations. The imputations are false. Even if some were clearly stated as opinions and were genuinely held by Professor Hazledine, they are not based on true facts and are not protected.

- 8 Foodstuffs, therefore, requests that the University amends the Article to remove these defamatory statements.

- 9 Provided these defamatory statements are removed by **5pm on 25 June 2024**, this will resolve matters as far as Foodstuffs is concerned.

Yours sincerely

Justin Graham / Tom Cleary

Partner / Senior Associate

Copy: Todd Somerville (Associate Director, Communications, University of Auckland, by email)
Sophie Boladeras (Media Adviser, University of Auckland, by email)

