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## SUBMISSION ON WHOLESALE SUPPLY INQUIRY PRELIMINARY ISSUES PAPER

- 1 Foodstuffs North Island (**FSNI**) and Foodstuffs South Island (**FSSI**) acknowledge the opportunity to comment on the Commerce Commission's (**Commission**) Preliminary Issues Paper (**PIP**) for its Wholesale Supply Inquiry (**Inquiry**) initiated under section 55 of the Grocery Industry Competition Act 2023 (the **Act**).
- 2 We comment on the themes arising in the PiP below and address certain specific points in the **Appendix**.

### **Executive summary**

- 3 We strive to provide an attractive and competitive regulated wholesale offering, and to comply with our obligations under Part 3 of the Act (which provides for the regulated wholesale regime). To date, our work on our regulated wholesale offerings has included regular engagement with the Commission and taking on board feedback the Commission has given on our respective offers.
- 4 Based on our work to date, and the PiP, we consider two underlying points to be of central importance to the Inquiry and the success of the wholesale regime as a whole. Working through these issues early in the process will assist all stakeholders (including RGRs, suppliers and customers, as well as the Commission) to more effectively direct their efforts and resources and provide greater guidance as to next steps for the regime. These are:
  - 4.1 the need to ground key stakeholders' (including the Commission, RGRs and suppliers) future work on the wholesale regime in a full assessment and clear articulation of costs and benefits. To date the regime has not been subject to a cost/benefit analysis, including during its development by the previous Government. Undertaking this analysis is required pursuant to section 57(3) and would, in practice, assist all stakeholders to best employ their resources in delivering under the regime (see from 6 below for further discussion),<sup>1</sup> and

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<sup>1</sup> Section 57(3) of the Act provides as follows:

*As part of an inquiry, the Commission must, when considering the matters under subsection (1)(b) or (c) [relating to whether additional regulation should be applied, and if so, what additional regulation],—*

4.2 as part of ensuring benefits outweigh costs, and the regime is doing what it is meant to, a clear link needs to be drawn between the purpose of the regime and how the Commission measures its success and considers future changes – such a link is missing from the PiP. For example, the wholesale regime has its genesis in the retail grocery market study in which the Commission commented that “*the absence of wholesale options limits constraint from small independent retailers and small new entrants*”. It remains appropriate to direct the wholesale regime and wholesale offerings with this purpose in mind, and to measure the regime’s success and any new proposals against the purpose e.g. testing whether availability, range and price remain a barrier to competition in light of retailers’ current ability to access products, and whether less, more or the same amount of regulation would assist (taking account of the expected costs and benefits) (discussed further from 14 below). More generally, articulating clear expectations for the regime will also assist with benchmarking and evaluating Inquiry findings and any recommendations (or other regulatory steps such as a Wholesale Framework or Wholesale Code) against what the wholesale regime can and should be trying to achieve, including by reference to costs and benefits. This is discussed further from 45 below.

5 The Commission has also identified certain matters as “fundamental issues with the RGRs’ wholesale offerings” in the PiP, which we address in more detail in the body of the submission:<sup>2</sup>

5.1 *The low volume of customers and sales through the RGRs’ wholesale offerings:* The regime has been in force for approximately a year, during which good progress has been made in its implementation. As with any new regulatory regime, a “bedding in” period is needed to accurately gauge the effects of that new regulation. In our view, it is too early to draw conclusions regarding efficacy (see below from 41 for further discussion).

In any event, both FSNi and FSSI are supplying products to a material number of retailers, and we are unclear on what number of customers or volume of sales the Commission expects to observe (including because, to our knowledge, no analysis on the total or potential market size, or current market dynamics, has been carried out). This issue highlights that the progress of the regime must be measured against realistic and proportionate (and transparent) expectations, based on the total size of the “addressable market” of smaller, new entrant and medium sized retailers (see from 14 below for further discussion of the target for the regime).

5.2 *The RGRs’ wholesale pricing models (including prices that enable competitively priced resale of goods):* We consider we comply with the Act’s requirements regarding our respective pricing models, including passing on scale and efficiency benefits and providing transparent pricing. [REDACTED]

(see from 24 below for further discussion of trade spend specifically, and from 58 in

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- (a) assess the benefits of applying (or continuing) different types of additional regulation; and
  - (b) consider what would be the most cost-effective type or types of additional regulation in the circumstances.

<sup>2</sup> At [30].

the Appendix regarding our respective pricing models). Based on our extensive engagement with the Commission on this issue, we have not received feedback that the Commission considers we are not compliant.

- 5.3 *Other grocery retailers' access to rebates, discounts and payments, including trade/promotional spend:* Trade spend is not a scale and efficiency benefit and is therefore not required to be passed on under the Act. It has always been understood that trade spend is separate from this requirement – this separation was a deliberate policy choice that is reflected in the Act. In our view, all rebates, discounts and payments related to FSNI and FSSI's scale and efficiency have and continue to be passed onto wholesale customers (trade spend is discussed further below from 24).
- 5.4 *Other grocery retailers' access to top-selling retail products:* Where a top-selling retail product is stored in our distribution centres and the supplier of the product has not opted out of the regime, the product is made available to customers. In many cases, direct supply offers retailers a more competitive option compared to RGRs' wholesale offerings, given relevant cost structures (see from 20 below). In other cases, the Commission's perceived gaps in RGRs' ranges are a result of supplier decisions to opt out of the regime, which we consider remains an important feature of the regime (see from 40 below for further discussion).
- 5.5 *The effectiveness of RGRs' systems and processes for wholesale supply:* We disagree that our respective systems and processes are ineffective, or otherwise not fit for purpose. We consider our systems are effective with a material number of customers currently being serviced successfully, and do not perceive our customers want us to increase the cost base of our wholesale offering to revamp these systems, at this stage. Of course, we always welcome feedback on this issue from our customers (see below from 65 in the Appendix).

### **Critical Considerations for the Inquiry**

#### ***Costs and benefits of interventions are a critical component of the Inquiry***

- 6 Unusually, no cost/benefit analysis has been undertaken in relation to the regulated wholesale regime, and this is a key gap in stakeholders' understanding of the regime's overall effectiveness, as well as that of any additional interventions.
- 7 The Commission remarked on this topic in the final report of the market study, stating:<sup>3</sup>
- formal cost-benefit analysis falls outside the scope of our study. Policy makers may undertake that analysis while developing or giving effect to any Government decision about recommendations that it may wish to take forward after considering our final report.*
- 8 In deciding not to make the wholesale access regulation a recommendation of the market study, the Commission noted:<sup>4</sup>

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<sup>3</sup> Commerce Commission, *Market Study into the retail grocery sector final report*, 8 March 2022, at [1.23].

<sup>4</sup> At [9.119].

*there are a significant number of issues that would need to be resolved before economic regulation would be feasible. Even if feasible, careful cost-benefit analysis would be desirable, beyond that which is within the scope of our study.*

- 9 At the time of the Regulatory Impact Statement (**RIS**), such work had not been carried out. The RIS notes:<sup>5</sup>

*the sources of information we used did not include much quantitative assessments of the costs and/or benefits of options.*

- 10 An additional RIS, focusing on the regulated wholesale regime specifically, also acknowledged the importance of weighing the costs and benefits of intervention, noting:<sup>6</sup>

*if the quasi-regulatory regime under-performs, the flexibility to choose from a range of tools (that also range in the degree of intervention) helps to recognise the dynamic nature of the sector and ensures that regulation is proportionate given the benefits and costs.*

- 11 As such, unusually for such a unique and intrusive intervention in commercial relationships, the wholesale regime has never been the subject of a full assessment of whether the anticipated benefits of the regime are expected to outweigh the anticipated costs. Furthermore, the intervention is novel and, to our knowledge, unique internationally, meaning an ongoing evaluation of the actual costs and benefits, compared to those that were originally anticipated, is appropriate.

- 12 In the context of the above, section 57(3) of the Act assumes particular importance. That provision requires the Commission (which could presumably be either the Commission or an independent economist on its behalf) to assess the benefits of applying (or continuing) different types of additional regulation, and to consider what would be the most cost-effective type or types of additional regulation in the circumstances. Even in a scenario where the Commission may proceed without completing a full Inquiry (Wholesale Code or Framework), the Act sets out process requirements and the Commission must reach and publish a draft and final determination. The potential costs and benefits of the proposed intervention must be a core part of that process, where the Commission is concerned to achieve the goals of the regime.

- 13 FSNI and FSSI are surprised the Commission's proposed approach to section 57(3) is not articulated in the PiP. This is a critical part of the assessment, both as a matter of compliance with the process laid out in the Act, and more broadly to ensure the appropriate use of the very significant resource being allocated to the regime (by the Commission, RGRs, suppliers and wholesale customers). FSNI and FSSI would be pleased to contribute further to this issue as the Inquiry progresses.<sup>7</sup>

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<sup>5</sup> MBIE, *Regulatory Impact Statement: Government responses to the Commerce Commission Grocery Sector Market Study* (June 2022), page 5.

<sup>6</sup> MBIE, *Regulatory Impact Statement Addendum: grocery sector regulatory backstop to the quasi-regulated wholesale access regime* (August 2022), pages 16-17.

<sup>7</sup> We note that the FSNI and FSSI information and data that would contribute to this analysis is likely to be largely commercially sensitive, and confidential. We appreciate the Commission is likely to be in a position to accommodate that sensitivity, but consider it worth noting.

***The wholesale regime targets the supply of smaller retailers including new entrants***

- 14 The wholesale regime is part of a package of measures to promote competition and efficiency in the grocery industry for the long-term benefit of consumers in New Zealand. Other measures include the introduction of the Grocery Supply Code, prohibition of restrictive grocery-related land covenants in the Commerce Act, introduction of the unit pricing regulations and increased Commission monitoring functions of the grocery industry. Each element of the regime has a particular focus.
- 15 While the Commission did not recommend the wholesale regime, the regime did originate from, and focus on, the Commission's finding in the grocery market study that "*the absence of wholesale options limits constraint from small independent retailers and small new entrants*". The Commission stated in its final report (emphasis added):<sup>8</sup>

*...we consider that larger grocery retailers which might seek to enter or expand in the retail grocery market in the future – such as Aldi, Costco and The Warehouse – are unlikely to use wholesale in the long term (or, for some, at all). This is because they would likely have sufficient volumes and scale to receive competitive pricing by purchasing directly from suppliers.*

*However, wholesale supply may be viewed as an attractive long-term mechanism for existing small independent grocery retailers and small new entrants to obtain the full range of competitively priced grocery products needed for them to provide a competitive offering comparable to the major grocery retailers.*

*In addition, retailers will often expand their offering (eg, number of stores or range of available products) over time after entering. Access to wholesale supply may help grocery retailers receive competitively priced supply of grocery products in the short-to-medium term, until they achieve a level of scale which allows them to receive competitive prices directly from suppliers.*

- 16 FSNI and FSSI agree with the Commission's framing in the market study of the potential opportunity in relation to the wholesale supply of groceries to retailers. That is, the regime is directed towards the supply of smaller and smaller new entrant retailers, and may assist them on their path to become larger competitors (rather than being a likely long-term solution for larger retailers). This is consistent with the commercial reality that smaller retailers are more likely to see and achieve value in a central wholesale offer, compared with larger retailers. While all retailers are permitted to access RGRs' wholesale offering, and FSNI and FSSI welcome customers of all sizes, obviously the assessment of the success of the regime and the basis on which the potential for any further regulation is considered, must take account of what it is aimed at, alongside a cost/benefit analysis.
- 17 The focus on smaller retailers is consistent with the fact that larger retailers are unlikely to benefit from RGRs' wholesale offerings in the same way, as they are able to obtain competitive offerings direct from suppliers, as the Commission itself recognised (see above). We also consider larger retailers (which may be in close competition with one or more RGRs) may be understandably reluctant to use RGRs' wholesale offerings if they do not have a strong need, to avoid supporting those RGRs.

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<sup>8</sup> At [9.88]-[9.90].

18 Separately, it is important that the Commission bears in mind that each Foodstuffs regional co-operative's offering covers only part of the country. While we are working to make our offers as attractive as possible, we appreciate it may be inherently less appealing to prospective larger national customers that we are unable to provide a seamless national offering. In this regard, we invite the Commission to feel free to take account of the relevant interviews, documents and information supplied as part of our recent merger clearance application.

19 The points set out above are relevant both to any future development of the regime, and to measuring its success. At its simplest, it would not be useful for the Commission to consider the regime a failure, or alter it, because it was failing to attract a large number of national customers, or large international entrants.

***In some circumstances, direct supply will be a more competitive option for grocery retailers***

20 There are scenarios where the cost structure of direct supply makes it inevitably more competitive than RGRs' wholesale offer. Put another way, there are products for which we cannot offer a competitive alternative to direct supply (from suppliers to grocery retailers). It is important that the Inquiry takes account of this reality. For example:

20.1 many fresh products, such as milk and bread, have a limited product life so it often makes more sense logistically for them to be supplied direct to retailers rather than via another retailer's distribution centre and network. If the Commission needs more information on this dynamic, please let us know, and

20.2 for products that are fast-moving and high-volume (e.g. toilet paper, bread, carbonated drinks), supply through a consolidated wholesaler (such as FSNI and FSSI) adds to handling costs and, therefore, product costs. Suppliers of such products tend to have their own well-developed and efficient distribution networks, meaning either suppliers would not wish to participate in our wholesale offering, retailer-customers would not find our offer compelling in respect of these products, or both.

21 In the scenarios described above, supply to FSNI and FSSI's own member stores often takes place directly from suppliers to stores, rather than from FSNI or FSSI distribution centres. This reflects the superior economics of that process. For example, a number of larger suppliers such as [REDACTED], have their own transport infrastructure, relationships with owner-drivers and relationships with small and medium sized retailers through which they supply direct.

22 These scenarios also mean we do not currently have sufficient physical infrastructure to bring all products into our distribution centres and networks. We would need to invest in additional infrastructure to do so. Requiring a very significant investment in additional distribution infrastructure, in order to create a de-optimised distribution network to force more products through it, is not consistent with the goals of the regime, and self-evidently the benefits would not outweigh the costs. Direct supply is an important and worthwhile feature of competitive wholesale supply.

23 Finally, these scenarios highlight that, as noted in the RIS, "*the lack of any 'essential facility' or 'natural monopoly' characteristic means that grocery wholesaling is not the type of*

*industry ordinarily regarded as potentially amenable to access regulation.*<sup>9</sup> Stepping back from the specific issues addressed in the PiP, the Commission appears to be focused not so much on ensuring the effective regulation of a particular “facility” or service but on securing grocery retailers’ access to *product pricing* on terms as close as possible to that achieved by RGRs. That being the case, a key focus is the allocation of trade spend, which is addressed in the next section.

***The allocation of trade spend is a key issue for discussion between the Commission and suppliers***

24 It is important to recognise that:

24.1 trade spend is spend by suppliers on positioning and promoting their products within retailers (i.e. competing). For example, in our experience, trade spend is often provided on a banner-by-banner basis as suppliers often seek different competitive positionings in the different banners,

24.2 trade spend is not a component of price that relates to RGRs’ scale and efficiency and therefore, not a discount, payment or rebate required to be passed through to wholesale customers under the Act. This was a deliberate policy choice,

24.3 given trade spend is linked to suppliers’ choice about how to position their products, the conversation about how best to address it within RGRs’ wholesale offers needs to occur between the Commission and suppliers themselves, and

24.4 given RGRs’ wholesale offers and suppliers’ direct offers are in competition with each other, it is appropriate for conversations about pricing components of suppliers’ role in RGRs’ offer to take place between the Commission and suppliers themselves, rather than with RGRs.

25 We elaborate on each of these points in the following sections.

***Trade spend is supplier competitive positioning, not a reflection of scale and efficiency***

26 Trade spend is not a component of pricing that reflects a grocery retailer’s scale and efficiency. As the Commission noted in the market study:<sup>10</sup>

*the price that grocery retailers pay suppliers for groceries, including any discounts for volume and economies of scale, only partially reflects the final net cost of those goods to the major grocery retailers. Suppliers also provide promotional funding (or trade and marketing spend) which can significantly reduce the retail price of goods.*

27 Consistent with the Commission’s findings in the market study, and the Act (including the legislative purpose of the regime in section 21), RGRs can be passing on to wholesale customers, in full, the pricing components that reflect their scale and efficiency, and yet the price at which they access the goods themselves might be different from the price that is available to wholesale customers.

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<sup>9</sup> *Regulatory Impact Statement: grocery sector regulatory backstop to the quasi-regulated wholesale access regime*, at [6a].

<sup>10</sup> Final report at [9.91].

28 Trade spend is not part of the scale and efficiency components of pricing that RGRs are required to pass on. The Commission's suggestion in the PiP that, "*it is not clear whether (or highly unlikely that) the benefits of the RGRs' scale and efficiency (including in the form of RDPs) were being appropriately passed on*" is at odds with the Commission's previous findings.<sup>11</sup> For completeness, we also note that both FSNI and FSSI have kept the Commission closely involved in the development of our regulated offers and, until the publication of the PiP, we had not heard any suggestion we were not complying with our obligations to pass on supplier price components that reflect scale and efficiency.

*FSNI and FSSI understand many suppliers (both in New Zealand and around the world) regard the allocation of trade spend among their retailer-customers as an important part of their competitive positioning*

29 Further, there are good reasons to consider the treatment of trade spend separately from the "base price", or price components that reflect the scale and efficiency of the retailer-customer.

30 The Commission recognised the importance of trade spend in the market study. It recognised both that improving wholesale prices may require that independent grocery retailers receive a significant portion of suppliers' promotional funding, but also that trade spend is a choice by suppliers rather than a feature that RGRs can or should control the allocation of among retailers.

31 That is, on the one hand the Commission recognised that:<sup>12</sup>

*any wholesale arrangement that does not address this issue [i.e. trade spend] is unlikely to result in wholesale prices to other grocery retailers lower than the retail prices charged by a large grocery retailer such as PAK'nSAVE, and is therefore unlikely to promote retail competition.*

32 The above could be read as consistent with the concern set out in the PiP regarding the margin available for wholesale customers to compete at the retail level.

33 On the other hand, the Commission also recognised that trade spend is a choice by suppliers to influence the competitive positioning of their products in particular retailers, so simply requiring RGRs to pass it through would not be appropriate. For example, the Commission has commented that:<sup>13</sup>

*Suppliers are willing to offer trade and marketing spend to some retailers because they expect that this will generate additional sales at the expense of competing products and brands. Therefore, some of the retail promotional activity we observe is driven by competition between suppliers rather than strong competition between retailers.*

*We have been told that promotional funding is offered by suppliers because it enables suppliers to differentiate their brands and compete for market share.*

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<sup>11</sup> At [45].

<sup>12</sup> Final report at [9.91].

<sup>13</sup> Final report at [5.131] and [8.107].



*Supplier-controlled promotional funding is a global dynamic and more pronounced with large multinational suppliers.*

- 34 The same supplier perspective was recently reiterated by the New Zealand Food and Grocery Council in its cross submission on the Commission's Review of the Grocery Supply Code:<sup>14</sup>

*there are many different types of promotional activities and they are used from time to time for a range of reasons, including to encourage consumers to trial a product, increase product awareness, increase volume during a lower demand period etc.*

- 35 This perspective is also demonstrated by the fact that suppliers often seek to negotiate different trade spend in different banners, rather than consistent trade spend across banners. While this is beyond FSNI and FSSI's direct knowledge, the ability to control trade spend may contribute (alongside superior economics) to some suppliers' desire to maintain direct links with retailers rather than participate in the wholesale regime.

- 36 The Commission was optimistic about the solution to this issue. It noted:<sup>15</sup>

*suppliers may directly enter into promotional funding relationships with independent grocery retailers, or in some cases may permit pass-through by the wholesaler. The feedback we have received indicates that supplier preferences may vary, but generally suggests a willingness on the part of suppliers to consider negotiating promotional funding with independent grocery retailers receiving wholesale supply from one of the major grocery retailers.*

- 37 The separation of price components associated with scale and efficiency (which RGRs are required to pass on in their wholesale offers) from trade spend is consistent with the policy decisions reflected in the Act. For example, the August 2022 cabinet paper regarding regulation of access to grocery wholesale and collective bargaining exemption notes (emphasis added):<sup>16</sup>

*The wholesale prices should allow the wholesale customer to enjoy the benefits of the major grocery retailer's volume and efficiency-based discounts from suppliers. The payment terms, any costs to serve, and any product margins should be transparent and consistent with a wholesaler operating in a workably competitive wholesale sector.*

*I recognise that retail prices at some major grocery stores may be lower than their wholesale offering prices due to the impact of retail-focused promotional and marketing discounts which are funded by suppliers.*

*It would not be reasonable to expect major grocery retailers to pass on these supplier funded discounts to wholesale customers without supplier agreement. Instead, I expect that generally suppliers will want to negotiate retail-focused promotional and*

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<sup>14</sup> New Zealand Food and Grocery Council, *Cross-submission on review of grocery supply code*, 11 October 2024, at [7.2].

<sup>15</sup> Final report at [9.92.2].

<sup>16</sup> MBIE, *Cabinet paper grocery sector reform: regulation of access to grocery wholesale and collective bargaining exemption* (August 2022), at [34]-[36].

marketing discounts directly with the wholesale customer. This could result in positive competition between retailers and benefits to consumers in the long-term. In either case, it should be the suppliers' choice.

- 38 For the reasons above, trade spend must be considered as part of the Inquiry, and needs to be considered separately from the components of pricing that reflect scale and efficiency.

*It is important and appropriate that the Commission seek a broad set of suppliers' perspectives on how trade spend can best be dealt with*

- 39 In addition, RGRs are competitors or potential competitors of suppliers in relation to the supply of grocery products to grocery retailers. That is, RGRs and suppliers are competitors at the "wholesale" level. So, while FSNI and FSSI can work with suppliers in relation to encouraging trade spend to be passed on (and FSNI has actively done so), or to encourage suppliers and grocery retailers to engage on trade spend, interrogating the issues and improving this aspect of the regime is more appropriately the role of the Commission and suppliers themselves. FSNI/FSSI are keen for this issue to be resolved and do not have a fixed view on how that is best done, but the key conversations to resolve it will be between suppliers and the Commission.

- 40 We consider it remains appropriate, and consistent with the policy behind the regime, that suppliers (including private label) ultimately retain their ability to choose whether or not they participate in the regime, and specifically, whether their products are made available through regulated wholesale offerings. This is consistent with the view adopted by Parliament in enacting the Act, that suppliers should have reasonable control over where their products are sold.<sup>17</sup> It is also consistent with avoiding inefficient cost in scenarios where it makes no economic sense for products to be directed to retailers via a RGR (see above at 20).

**Early days for the regime, with good progress made to date**

- 41 The Inquiry proposes to assess the efficacy of the wholesale regime after approximately a year of it being in force. The regime has required FSNI and FSSI to develop entirely new business lines to comply, and this has been a significant undertaking. The undertaking has been carried out in a context where, as cabinet has acknowledged, "*regulation of access to grocery wholesale is unprecedented and requires a novel approach*".<sup>18</sup>
- 42 FSNI and FSSI have invested and acted swiftly to deliver regulated wholesale offerings and have continued to adapt and scale up these offerings. Further, as noted above, the Commission has been closely and deeply involved in the development of FSNI and FSSI's offerings, and therefore has had the opportunity to assist with compliance and improvement throughout. It is too soon to say what the potential of the regime, including results from what has been achieved to date, will be under the current regulatory settings.
- 43 Further, FSNI and FSSI (with input from the Commission) have made good progress to date, securing material sales and customer numbers. FSNI's results show the scaling up

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<sup>17</sup> See for example, the Economic Development, Science and Innovation Select Committee, *Grocery Industry Competition Bill*, at page 10.

<sup>18</sup> *Cabinet paper grocery sector reform: regulation of access to grocery wholesale and collective bargaining exemption* at [12] and [37].

and increased momentum of its wholesale offering. For example, it has experienced a 41% increase in ordering customers during the three months ending September 2024.

- 44 FSSI runs its wholesale offering through Trents. It already supplies over 1,200 grocery retailers and foodservice retail providers such as canteens, convenience stores, service stations and dairies (as well as some of the 72 On the Spot stores), plus its wholesale access customers. These are all smaller retailers reflecting the fact that FSSI is already active in supplying groceries to smaller retailers in the South Island. We note that FSSI has experienced minimal demand for its wholesale offering to date – as we believe the Commission is aware, this does not reflect a lack of effort on FSSI’s part, nor flaws in the regime, but reflects the size of the South Island and the fact that many smaller retailers already have secure wholesale supply (including from FSSI) which meets the needs of their businesses and cash flow operations.

**Increased focus on realistic expectations of the wholesale regime would assist with ongoing progress**

- 45 FSNI and FSSI have supported the wholesale regime since before it was introduced. As the Commission is aware, we are working to make our offers both compliant with the Act and commercially attractive, and are being transparent and collaborative with the Commission in doing so.

- 46 In our view, one of the most beneficial additions to the current work on the regime would be to ensure stakeholders are clear on the realistic and proportionate expectations for the regime, including at a practical level, taking account of the costs and benefits of the work required, the nature of the retail grocery market in New Zealand and in light of the existing wholesale markets used by retailers.

- 47 The terms of reference for the Inquiry refer to the goals of the regime, and issues with the current offerings. There are also several places in the PiP where the Commission has indicated what it would “expect” to see in a competitive wholesale market, or has suggested a problem may exist. However, in many cases it is unclear why the Commission’s expectations are considered realistic in the context of the wholesale supply of grocery products, and therefore why a particular issue/recommendation might be regarded as a problem/solution. This is compounded by the absence of a cost/benefit analysis.

- 48 A clearer focus by the Commission and the Inquiry on the realistic expectations for the wholesale regime would allow for a focus on constructive and proportionate solutions being recommended. This is particularly the case given:

48.1 the Commission did not recommend the wholesale regime following its market study, so it has not had the opportunity to offer detailed guidance on what the regime should be aiming to achieve, and

48.2 the previous Government did not undertake a cost/benefit analysis when the regime was proposed and developed.

- 49 At worst, without a clear understanding of what the wholesale regime is trying to achieve, RGRs, suppliers, wholesale customers and the Commission could misuse time and resources. Realistic and credible goals, which take account of anticipated costs and benefits and the intended focus of the regime, and are consulted on and clearly communicated to stakeholders, are critical.

### **Inquiry recommendations and further regulation**

- 50 The Commission's Inquiry findings and any recommendations to the Minister for further (or for reduced) regulation (or other regulatory steps the Commission may take without needing to make recommendations to the Minister, such as a Wholesale Framework or Wholesale Code) must be benchmarked against a clear sense of what the wholesale regime can and should be trying to achieve, including by reference to costs and benefits. Without this, there will be no way of knowing whether further action and/or further regulation is likely to address the overarching purpose of the Act, to promote competition and efficiency in the grocery industry for the long-term benefit of consumers in New Zealand, in a timely, effective and cost-efficient manner (that does not embed structural inefficiencies).
- 51 For example, imposing specified access terms on RGRs that do not take into account the particular group of potential customers that the regime is directed towards serving (being smaller and medium sized retailers) and the related market size and market constraints could lead to offerings that are not fit for purpose. Additionally, without a cost/benefit analysis to inform decision-making, imposing specified access terms could be ineffective as a form of further regulation, with a disproportionate impact on all stakeholders and without ultimately improving retail grocery competition and end prices for consumers.
- 52 Of course, where the Inquiry is being conducted neutrally and with an open mind, it is appropriate that there is no presumption that it should or will result in further regulation. We agree with the Commission's statement in the PiP:<sup>19</sup>

*As part of the Inquiry we will also be considering whether any other regulation or action may be necessary or desirable to promote the purpose of the Act.*

*This will include assessing whether new or amended legislation/regulation would help, as well as whether there are non-regulatory actions that would help. The outcome of this will likely be a recommendation to the Minister for their consideration.*

### **Procedural considerations for the Inquiry**

- 53 The matters the Commission identifies in the PiP are complex and relate to the separate operations, and collective dynamics and interactions of wholesale customers, suppliers and RGRs. We appreciate the adequate time given for comment on the PiP.
- 54 However, FSNI and FSSI consider the lack of a cross-submission phase is a serious shortcoming in process, given it removes the opportunity for stakeholders to engage with each other's views and suggestions.
- 55 This is particularly the case given the PiP was released before the Commission had completed its consultation on the terms of reference. We had planned to comment on the terms of reference shortly after it was released, and within the timeframe initially indicated. Before we could do so, and without forewarning, the Commission released the PiP. That procedural error makes it even more important that the Commission does not dispense with its usual approach of allowing submitters to comment on matters raised in submissions. We were concerned by this unannounced change in process, which meant we had no opportunity to comment on the terms of reference.

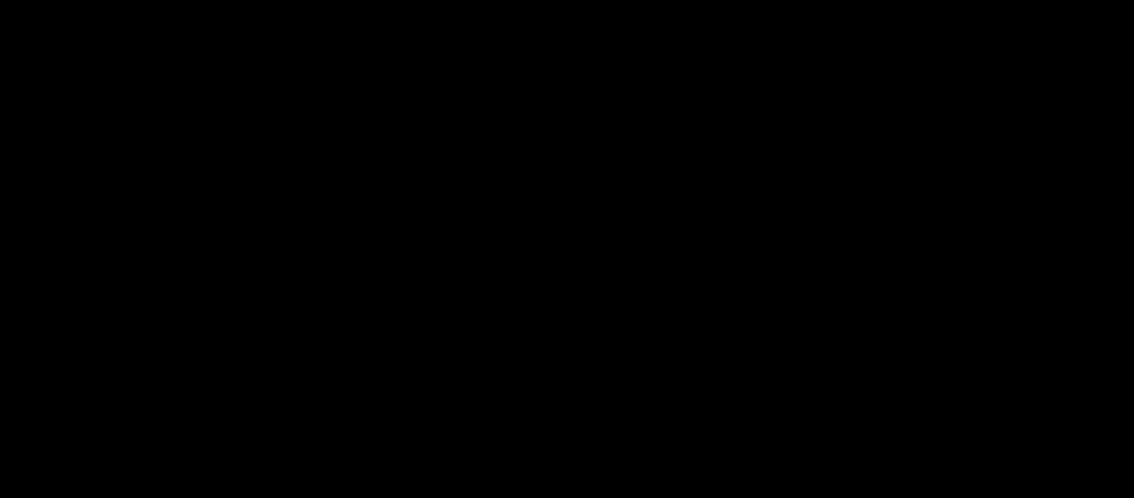
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<sup>19</sup> At [116].

**Next steps**

56 Please do not hesitate to contact us if you have any questions regarding this submission.

Yours sincerely



**APPENDIX**

**Wholesale pricing**

57 Please refer to the discussion above from 24, regarding trade spend.

58 In relation to its wholesale pricing, FSSI notes that it:

58.1 [REDACTED]

[REDACTED]

(b) [REDACTED]

[REDACTED],

58.2 [REDACTED], and

58.3 [REDACTED], and

58.4 [REDACTED].

59 FSSI considers its wholesale pricing complies with the Act (and, as above, has not heard differently based on its engagement with the Commission to date) by:

59.1 providing transparent pricing,

59.2 passing on scale and efficiency discounts, payments and rebates from suppliers,

59.3 charging a cost to serve that accurately reflects the costs of getting the product to the customer. FSSI notes that freight accounts for a significant portion of the costs

[REDACTED]

associated with regulated wholesale supply, especially for small orders (see below from 69 for further discussion of minimum order requirements), and

- 59.4 earning a small margin, which in part contributes to the costs of assets (such as distribution warehouses and trucks) used in the provision of its regulated wholesale offer.

### **Product range**

- 60 In FSNI's experience, the gaps the Commission perceives in range predominantly occur where suppliers' products/types of products are not stocked in its distribution centres through which it fills its wholesale orders (see also the discussion above at 20, regarding direct supply), as well as supplier opt-outs. FSNI consistently reviews its offer and continues to develop and evolve its range.
- 61 FSSI considers the gaps the Commission perceives in range are largely attributable to supplier opt-outs. FSSI has received strong feedback from some suppliers that they already have direct channels to retailers and prefer to supply through these direct channels.

### **Fresh produce**

- 62 Fresh produce is already competitively supplied direct to retailers or purchased from wholesale markets. The Commission has acknowledged that:<sup>21</sup>
- 62.1 fresh products "are often available through specialty wholesalers (eg, T&G Fresh) and other alternative channels of supply",
- 62.2 wholesale customers have shown "mixed demand for products in fresh categories", and
- 62.3 "smaller and specialty retailers who stock fresh categories generally preferred their current channels of supply".
- 63 Competitively supplying fresh produce is complex given the limited shelf life of products and costs associated with their transport (e.g. cool storage). FSNI does not currently perceive demand to extend its offer to include fresh produce, noting that doing so would add cost and complexity to the offer, which FSNI can provide more information on as required). It notes that it has only received [REDACTED] queries regarding fresh produce in expressions of interest received from prospective customers.
- 64 FSSI offers a small core range of fresh produce (such as potatoes, onions, carrots and apples) as part of its wholesale offering. In FSSI's view, expanding this range would incur the cost and complexities described above. It also notes that it has experienced very low demand for fresh produce and that in the South Island, there are multiple fresh wholesalers servicing retailers directly.

### **Systems and processes**

- 65 FSNI and FSSI disagree with the Commission's view in the PiP, that there are fundamental issues with the systems and processes in place for our wholesale offerings. Further, given the challenges with providing an offer on attractive price terms, we expect the Commission to be cautious about adding significant cost to the offer without a clear anticipated benefit.

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<sup>21</sup> Commerce Commission, *Annual Competition Grocery Report 2024*, 4 September 2024 at page 100. The Commission reiterates in the PiP at [61.3] that "we recognise there is mixed demand for fresh products through regulated wholesale and fresh products are often available through specialty wholesalers".

66 FSSI uses Trents' existing e-commerce portal for the management of its wholesale orders. Approximately [redacted]% of orders are made through this portal. Over [redacted] customers regularly use this platform. FSSI rejects the suggestion that these systems and processes are inadequate.

67 FSNI utilises existing systems and processes for its wholesale offering, which have been tested and used elsewhere in its business. We believe our systems and processes are effective, as evidenced by increasing customer engagement through orders. We will continue to develop and adapt these systems and processes over time as our offering develops.

68 [redacted]

**Terms and conditions**

***Minimum order thresholds***

69 The Commission notes in the PiP the impact of minimum order requirements on prospective and existing customers' ability to make orders. While we acknowledge that this may be a point of difficulty for some customers, it is a necessary requirement to make our wholesale offerings viable and price competitive in the long term. That is, without these minimum order requirements, the costs of meeting orders are vastly outweighed by what customers could expect from a competitive offer (or can reasonably be expected to pay for those orders).

70 FSNI and FSSI note that their respective minimum order thresholds have been set at a level that aims to maximise wholesale customers' ability to access its offer (by keeping the thresholds down), while avoiding adding material costs into the distribution network as a whole (to avoid flow on effects of increased costs, for themselves and their wholesale customers).

***Order forecasting***

71 In FSSI and FSNI's experience, forecasting can also prove difficult for some retailers. That is, many small and medium sized retailers buy product on a week-to-week basis, rather than forecasting.