HABILIS

Submission: FSNI-FSSI merger

Response to Statement of Preliminary Issues | 31 January 2024 | v1.0

Introduction

He tina ki runga, he tāmore ki raro.

In order to flourish above, one must be firmly rooted below.

This submission is made in response to the merger application made by Foodstuffs North Island Limited and Foodstuffs South Island Limited. We are opposed to the merger on the grounds that it will significantly impede the resolution of the market failure being experienced in the grocery sector, which in turn is the result of the Commerce Commission's regulatory failure. Further, the merger will consolidate the industry further with a high likelihood of adverse market outcomes for customers, and increase the barriers to entry for new competitors. We note the sole beneficiary of the merger will be the merged entity.

We continue to take issue with the Commission's management of the process, particularly the lack of disclosure of important information, the over-reliance of commercial confidentiality, and the lack of effective application of the public interest test in s9(1) of the Official Information Act 1982.

Our document is therefore in two sections:

1. **Issues about the process** deals with the Commission's failure to provide sufficient information and a short timeline for interested parties to provide an informed submissions.
2. **The substantive matter** of the acquisition itself, which will result in adverse market outcomes if approved, but which provides a range of options for the Commission to consider that can address the challenges.

We ask that the Commission considers the options set out in this paper, adopts Option 2, and proceeds with a full assessment of the merger on that basis.

About us

Habilis New Zealand Ltd provides consultancy and advisory services to regional Aotearoa, including strategy development, economic and social impact modelling, business case and investment proposal development, stakeholder engagement and communications, and benefit and impact analysis. Our client base includes iwi, NGOs, local government and the private sector.

Habilis NZ Ltd is based in Tāmaki Makaurau.

Issues about the process

On 18 January 2024 the Commission released a Statement of Preliminary Issues (SOPI) on the proposed merger of Foodstuffs North Island Limited (FSNI) and Foodstuffs South Island Limited (FSSI). The Commission invited submissions from all interested parties.

The timeline issues

We note that the Commission continues to provide extremely short time windows for interested parties to provide submissions on major mergers, whilst consistently missing its own timelines.

The Commission's Merger Assessment Guidelines (MAGs)[1] note in paragraph 6.106 (page 49), the SOPI is due for release some 5 working days after the application is received. As the documents show, the application from Foodstuffs was received on 14 December 2023, yet the SOPI was not released until 18 January 2024, some 17 working days later, allowing for the Christmas shutdown period.

This is an unfortunate continuation of the Commission's inability to meet its own timelines. We note the Commission's comments in the media[2] that:

> A spokesperson for the commission (it declined to put a name behind its comments) said the statement of preliminary issues Duston was referring to summarised the applicant's views from their application, along with the commission's preliminary views on those areas seen as needing to be tested during the investigation.
>
> "The statement of preliminary issues is not a reflection of any views held by the commission, but rather a document designed to help people understand what the commission considers will be relevant to the analysis it needs to undertake."

These comments – and the documents themselves – indicate a minimal level of analysis from the Commission; most information in the SOPI is simply copied from the application into a standard Commission template. The organisation apparently has some 400 staff[3], so it is hard to understand why this mechanical process needs to take 17 working days, more than 300% of the allowable time window.

And we note that the time taken by the Commission to construct the SOPI is 70% longer than the time it provides to the rest of the country to respond to it.

This is a repetition of the systemic failings in the Commission's engagement model. For whatever reason, the Commission seems to assume the private sector is willing and able to drop whatever it is doing to provide input to the Commission in major matters; the Commission has done this time and time again. There seems to be a Wellington bureaucratic conceit that the timelines of whatever process agencies are currently running will be the most important agenda item for every organisation and individual in the country.

It's deeply disappointing that the Commission continues to think it is the only organisation that should enjoy the luxury of reasonable deadlines.

The analysis shortfall

It's also disappointing that the Commission's supporting material for making an informed submission is so heavily redacted, to an even greater degree than seems to be the norm. Whole sections of the document have been removed from the Application, making it of dubious value in places.

It is not at all clear why the Commission has allowed such a wholesale withholding of key information. As the Commission's statements in the media[4] note:

> Regarding its habit for redacting commercial information, the Commerce Commission said it had to be a responsible steward of confidential information and it could only effectively perform its investigative function if businesses had the confidence that confidential information would not be generally disclosed to the public.

However, the process by which redactions are made – and by whom – is entirely opaque. Further, there is no evidence that the public interest test embedded in the Official Information Act 1982 has been applied. As guidance from the Ombudsmen[5] notes:

> The grounds for withholding official information in section 9 of the OIA are subject to a 'public interest test'. This means agencies must balance the public interest in disclosing information against the need to withhold it. If the public interest in disclosure outweighs the need to withhold the information, then it must be released.

We note that the Commission's obligations under the Official Information Act 1982 supersedes mere stewardship or contractual arrangements for commercial confidentiality, and that the Ombudsmen have extensive guidance and case studies to assist the Commission with making more balanced decisions on these matters.

The equity shortfall

As is a continuing challenge, there has been no attempt by the Commission to address any of the equity issues inherent in its process. Foodstuffs has obviously had many months to prepare the application and has the financial wherewithal to engage some of the country's best legal and consulting firms to do so. In comparison, other interested parties are being given a mere two weeks to make a fulsome submission addressing complex issues around market failure – and even if they have the financial resources to engage similarly qualified professional assistance, the odds of being able to obtain the necessary personnel within a two week window are low. This is highly prejudicial to the public interest.

Further, we are concerned with the Commission's engagement focus on the industry, to the exclusion of other market participants. In public statements[6] the Commission notes:

> For each merger we carry out a detailed analysis of the affected markets, and **seek input from a wide range of industry participants** to assist us in our overall consideration of the extent to which the transaction in question is likely to substantially lessen competition in any market [emphasis ours].

It is not at all clear why the Commission maintains an exclusive focus on engaging with the very participants that are – in the case of the grocery sector – enjoying windfall profits and unjust enrichment at the expense of consumers. All markets are obviously

made up of two parts; willing sellers and willing buyers. Yet the Commission's proactive engagement around mergers and acquisitions – and indeed within market studies – seems prejudiced against the buyer side of the market. This is highly exclusionary and is clearly resulting in adverse outcomes.

As is the case with practically every other submission process run by the Commission, the major market participants are being granted the time and resource to make thorough and well reasoned arguments, whilst all other market participants and the general public – who will inevitably pay the costs of anti-competitive mergers – are being restricted to short windows and inadequate information.

This has the effect of making the competition issues being considered by the Commission the preserve of a select few insiders. It appears that unless parties are competition lawyers – or have engaged competition lawyers – then the odds of successfully negotiating the processes and timelines are low. Perhaps the reason for the processes being run as an exclusive club for the legal profession is that a considerable proportion of the Commission's management is made up of former competition lawyers.

The likelihood of poor outcomes

As is clear from the way the Commission is running the submission process, it once again appears to be consultation theatre – that is, it provides the illusion that consultation has occurred, whilst erecting every conceivable obstacle to meaningful engagement with parties other than the applicant. The purpose of the process is clearly to enable officials to tick a compliance box, whilst not burdening themselves with too much work.

This unhelpful bureaucratic approach has led to invidious outcomes for Aotearoa. We note from the Commission's case register that no merger application has been declined since March 2018, indicating the process is merely a compliance way-point with no believable likelihood that regulatory intervention will occur. We strongly suspect the Commission has begun measuring its KPIs by the number of merger applications successfully approved, rather than by whether there are vibrant and effectively operating markets for goods and services in Aotearoa; in other words, the Commission's only goal is process efficiency, not societal outcomes.

And as a result of the Commission's inaction to prevent excessive market consolidation, oligopolies have formed. These include the very grocery sector that is the focus of this application. In each of these failed markets there are a small number of outsized participants engaging in the systematic abuse of their market power, to the detriment of the country.

As the Commission's own market studies show[7], these oligopolies are levying super-profits at the expense of consumers, to the tune of many billions of dollars a year. And as many of the participants are overseas owned, the excessive profits are imposing a further deadweight drag on Aotearoa's economy, to the detriment of whānau, businesses, farms, and our wider national wellbeing.

Unfortunately, the Commission has been entirely remiss at addressing these oligolopic behaviours, even though it has the legislative tools, the political mandate and the moral obligation to do so. The Commission has taken no legal action to break up any oligopoly since 2012, and it seems simply unbelievable that there has not been a single instance of the abuse of market power in that period. Yet despite the clear and obvious evidence of unjust enrichment at an industrial scale in vital markets, the Commission seems determined to never trouble the courts.

In fact, as the case register demonstrates, the Commission has been the primary architect of the undue consolidation and the resulting market abuses. The mergers in the grocery sector that have led to the current duopoly have not been an accident; the Commission has been a willing and enthusiastic midwife throughout the process.

Summary

It is apparent that the country can have little confidence in the actions of the Commission, because:

1. The time window for providing submissions is too short, and the Commission continues to consistently miss its own internal deadlines for preparing SOPI documents and making information available in a timely fashion.

2. The information supplied by the Commission to enable other market participants and the wider public to make an informed submission is woefully inadequate due to heavy redaction of the Application, with no evidence of a public interest test being applied.

3. Even if interested parties navigate the inherent inequities in the Commission's processes, its track record indicates that approval for the merger will be given in 100% of cases, irrespective of the subsequent adverse outcomes.

4. The Commission's track record also indicates that it will never take action to break up the oligopolies that form as a result of the mergers, nor to punish the unjust enrichment of participants that results.

It is therefore evident that the Commission is failing Aotearoa in the area of competition policy and enforcement. The consequential market failure implications of the regulatory failure will be explored in more depth in the following section.

Substantive matters

Executive summary

Foodstuffs asserts that the merger of FSNI and FSSI will have no adverse market outcomes. Sadly, we agree – but this is solely due to structural market failure in the grocery sector, which has been enabled by the Commission's regulatory failure.

As the Commission notes in the SOPI:

> We determine whether a merger or acquisition is likely to substantially lessen competition in a market by considering what would change with a merger. We do so by comparing the likely state of competition if a merger proceeds (the scenario with the merger, often referred to as the factual), with the likely state of competition if a merger does not proceed (the scenario without the merger, often referred to as the counterfactual). This allows us to assess the degree by which the Proposed Merger might lessen competition.

However, this statement assumes that there is a functioning market in the grocery sector, shaped by competition, which the merger could affect in some way. This is clearly not the case; there is merely a duopoly, characterised by the exploitation of both suppliers and customers by the two supermarket giants. There is negligible effective competition, something noted in the Commission's own market study.

And it is glaringly apparent that there can be no adverse competition effects from the merger within a market that has no effective competition. So based on the test outlined above, the Commission must approve the transaction.

The problem is exacerbated by the Commission's fixation on the current definitions of factual and counterfactual. Within a failed market, these two things are identical; the country will be suffering the effects of systemic abuse of market power irrespective of the corporate structures of the abusers. Merging entities, changing the names over the doors or even rationalising to a single monopoly will have no discernible impact on the level of failure, or on its adverse effects on consumers.

However, a failed market is not the outcome the country wishes – even if it is the outcome the Commission's indifferent performance over the last two decades has gifted us. So the fundamental question is how the restoration of a functioning market in the grocery sector will be either enabled or impeded by the proposed merger.

The challenge in assessing the proposed merger using this approach is that it requires the Commission to think about markets differently. It needs to:

1. Accept that the grocery sector is a failed market due to regulatory failure.
2. Acknowledge that market failure is producing adverse outcomes for Aotearoa that require rectification.
3. Assess the merger based on its ability to aid or hinder that rectification.

These matters are discussed in more detail below, along with noting our strong scepticism that the Commission has the analytical frameworks, policy development or intestinal fortitude to take the required course of action.

Market failure

The Commission has obviously conducted a market study into the grocery sector, which notes the duopoly that stands astride the sector, the excessive profits, and the low likelihood that the barriers to entry and scale can be overcome by new competitors.

The market study also made recommendations that resulted in new legislation and the freshly-minted Grocery Commissioner. In our view this is a textbook case of bureaucratic magical thinking, hoping that the essential nature of the two duopolists would change simply because of some additional headcount at the Commission. While it's early days, it's already clear there has been minimal impact on the supermarket bills of Kiwis, and there is certainly no indication that the grocery sector is any more competitive since the Commission commenced the study, nearly four years ago.

A useful definition[8] of a monopolist is "companies that can act independently without needing to consider the responses of competitors, customers, workers, or even governments." This certainly applies to both Foodstuffs and Woolworths – there is strong evidence that the duopolists can act unilaterally on pricing, product and profit, with impunity.

There is no sense that this dynamic will change in the near future. As noted, the recent legislative changes have had no discernible effect on the level of competition to date, and the changes to market structure – restrictions on land use, some voluntary wholesaling obligations – are so timid that they will not result in any structural market reform. For the purposes of the SOPI, then, it is reasonable to assume:

- The grocery market has failed; and
- That failure will continue into the indefinite future, in the absence of new regulatory intervention.

Aside: an ode to Chapman Tripp

It appears from the papers that Chapman Tripp prepared the Application on behalf of Foodstuffs. In our view and without the slightest trace of irony, they've done a masterful job.

As noted, it's apparent even to the untutored observer that their client is a duopolist in a failed market, making excessive returns by exploiting their market power to extract unjust enrichment from suppliers and consumers alike. It's also clear that the proposed merger will have exactly zero effect on the competitive landscape in the grocery sector, because the essential nature and market power of the duopolists will remain unchanged from the transaction.

So Chapman Tripp have had to weave a very difficult course indeed; they have to state the obvious – that the merger will have no effect on competition – whilst also avoiding stating the obvious; that the reason there will be no effect on competition is because their client is a duopolist.

Throughout the Application document – even bearing in mind the extensive and unhelpful redactions – Chapman Tripp artfully thread a course between these two diametrically opposed ideas. At no point do they admit to anti-competitive behaviour in a failed market, whilst managing to provide a robust argument for why there will be no adverse competition outcomes.

The team who has worked on this masterclass in ducking and weaving past the reefs and shoals of legal difficulty are to be commended. We would definitely trust them to make the Kessel Run in under 12 parsecs[9].

Market failure and the competition test

As noted above, the competition test applied by the Commission assumes there is a functioning and competitive market in the grocery sector; this is plainly not the case.

The basic competition test defined in the SOPI is therefore of no use in assessing the effects of the merger in a failed market; and unfortunately, there is little evidence that the Commission has developed the thinking or analytical approaches necessary to deal with the effects of mergers and acquisitions in failed markets. Had it done so, we would have expected to see the results of the different methodological approach in the SOPI, rather than simply a repeat of the standard boilerplate.

The standard tests are given as follows:

1. How much actual or potential competition between the Parties could be lost as a result of the Proposed Merger – in other words, the extent to which the Parties compete with each other today, or might be likely to compete with each other in the future in the absence of the Proposed Merger;
2. Constraint from existing competitors – the extent to which current competitors compete and the degree to which they would expand their sales if prices increased;
3. Constraint from potential new entry – the extent to which new competitors would enter the market and compete if prices increased, quality reduced, innovation declined or other elements of service or competition reduced (e.g., worse or less frequent promotions);
4. The countervailing power of customers in markets in which the Parties wholesale supply grocery products – the potential constraint on the merged business from a wholesale customer's ability to exert substantial influence on negotiations and whether any countervailing power of wholesale customers might increase or decrease with the Proposed Merger; and
5. The countervailing power of suppliers of grocery products to the Parties in markets in which the Parties acquire grocery products, compared to any buyer power of the Parties themselves – the potential constraint on the merged business from a supplier's ability to exert substantial influence on negotiations and whether any supplier power might increase or decrease with the Proposed Merger, or whether the Proposed Merger would strengthen the buyer power of the Parties.

As the Application notes – in somewhat cautious language – these questions practically answer themselves in the context of a failed market. They are:

1. Lost competition – none, as they don't compete
2. Constraint from existing competitors – none, as there's a functional duopoly
3. Constraint from new entrants – none, as there won't be any new entrants
4. Power of customers – none, as there's a duopoly in a failed market
5. Power of suppliers – none, as there's a duopoly in a failed market.

If these tests are applied in their unaltered state as proposed by the Commission, they will inevitably result in the merger being approved – which, in turn, will result in the existing market failure in the grocery sector becoming further entrenched. This is the adverse outcome that needs to be avoided from a consumer perspective.

It is entirely clear that a failed market is not in the best interests of Aotearoa New Zealand. The lack of competition that was extensively documented in the market study is having a pernicious effect on consumers and businesses, and exerting a deadweight drag on the economy as a whole. Perpetuating this state of affairs will do our people and our country no good at all. Accordingly, the Commission needs to assess the viable options for how the adverse effects can be avoided.

The available options

There are three options available to the Commission for how it proceeds with the Application:

1. Option 1: Extend and Pretend – pretend there is no market failure and apply the standard competition test on its merits. As the failed market will not be taken into account, the analysis will demonstrate there are only minimal competition effects, which in turn will result in the merger being approved and the duopoly being further entrenched. This will strengthen the current oligopoly and double down on the harms already being experienced by consumers.

2. Option 2: Acknowledge and Prosecute – apply the current competition test, which will result in the merger being approved on the basis of its minimal competitive impact, but explicitly acknowledge the market failure identified in the market study. This approach admits that the failed market leads inevitably to the merger being approved. However, the admission of market failure also leads to the conclusion that Foodstuffs has thoroughly abused its market power, which the Commission addresses by bringing an immediate prosecution under s36 of the Commerce Act.

3. Option 3: Assess the Test – evaluate whether the standard competition test used by the Commission is actually fit for purpose in a failed market, and revise the criteria to ensure that the ending of consumer harm and the restoration of competition in the grocery sector is actually the test applied. In this case, the merger is declined as it will further entrench the existing duopoly and will act as a further obstacle to new entrants. Use of altered conditions can be tested in the courts.

Each of these options is examined in more detail below.

Option 1: Extend and Pretend

This option represents the continuation of the Commission's current course and speed. It relies significantly on some magical thinking from officials; namely, that the failed market and duopoly powers of Foodstuffs and Woolworths are immaterial to the consideration of competitive impacts from the merger.

Under this option, the Application is assessed using the tests set out in the SOPI. As noted, the highly likely result is that the merger will be approved because the competitive impacts are minimal, both for the current state and the likely future state. And in fact the future state – a duopoly with excessive market power – will look very similar to today, effectively vindicating the Commission's competition analysis.

We think this is the most likely outcome, for the following reasons:

1. It appears that the Commission has neither the conceptual framework nor the policy tools to assess failed markets. The cognitive straitjacket the Commission has built for itself assumes that all markets are functional and work well; there seems to be little evidence that failed markets are recognised or acknowledged.

2. Given this is the case, there are few policy or operational tools available to chart a path from oligopoly to competition. Searching the Commission's website reveals very little about failed markets or oligopolies, and the entirely timid recommendations in the market study – some additional staff at the Commission, voluntary agreements – does not inspire confidence there are robust policy prescriptions waiting in the wings.

3. There is little appetite within the Commission for opposing mergers. As noted above, 69 out of the last 70 mergers have been approved, and there has been no decline of a merger since March 2018. The Commission points out that applications have been withdrawn on advice from officials, but that's immaterial in this case as Foodstuffs has elected to proceed with the Application.

4. The Commission is likely to see the application of the existing competition tests as low risk from a reputational standpoint. It will be able to point to the well-travelled legal and administrative path that uses the current tests, and may well claim that its legislative and political hands are tied, despite making no efforts to untie them.

The core challenge with the Commission choosing this option is that it prioritises process over outcome; that is, it allows the Commission to tread a well-worn procedural path to exactly the wrong outcome for the country. It is not in the national interest for the current duopoly to be further strengthened and entrenched, but unless the Commission sees its mandate as prioritising the restoration of a competitive market in the grocery sector, it will make exactly the wrong decision regarding this merger.

Option 2: Acknowledge and Prosecute

Under this option, the Commission continues to use the existing competition tests, with the expected outcome that the effects of the merger are minimal and it is approved. In effect, this is the same as Option 1. From a procedural perspective, this option assumes the competition tests have legislative primacy and will not survive challenge in the courts; that is, they cannot be varied in any way and must be applied as written in the SOPI.

The difference is that the Commission explicitly acknowledges the failed market in the grocery sector and the fact that Foodstuffs is one half of a duopoly as part of the process; this will largely confirm the findings of the market study, albeit in more black and white terms.

The acknowledgement of harms to consumers through market failure then becomes the stepping-off point for prosecution of Foodstuffs post-merger, for its historical and ongoing abuse of market power. The Commission has all the powers it requires to do this under s36 of the Commerce Act. However, we think the Commission is unlikely to take this course of action, for the following reasons:

1. The Commission may think that its restatement of the grocery sector as a failed market dominated by a duopoly steps beyond the carefully framed conclusions in the market study – and that's likely to be the case. Given the level of timidity from officials, this is probably a waterline issue for the Commission; it may well feel that reaching a stronger conclusion less than a year after a legislative change carries too much reputational exposure, as if the Commission's reputation was still intact despite the adverse impacts being felt by the country at the supermarket checkout.

2. The Commission has no track record of equivalent prosecutorial action. As we've previously noted, the last time any corporation was dragged into court by the Commission for the abuse of market power was way back in 2012, and this is

despite the obvious abuses that are taking place in everything from the grocery sector to the banking sector. The Commission's lack of intestinal fortitude at both the governance and management levels to take court action is puzzling, but it does prejudice against this option being attractive to the Commission, based on its track record.

It's worth noting that the threat of prosecution may well act as an incentive for Foodstuffs to withdraw the application. Should the Commission indicate that approval of the merger would also mean a court case challenging the abuse of market power and seeking the full range of damages available under the Commerce Act, Foodstuffs might well form the view that some operational efficiencies achieved by the merger are not worth the fight.

However, such a threat would need to be credible, and based on the Commission's track record and current messaging, we don't think it is.

Option 3: Assess the Test

The two prior options both assume that the competition test applied in the SOPI is used to assess the merger application. This option assumes exactly the opposite – that the competition tests are amended to reflect the fact that the grocery market has failed and is now dominated by a duopoly.

In these circumstances, different criteria can be used to assess the impact of the merger. Acknowledging the market failure is the starting point, which then allows the Commission to set out an objective of the restoration of a competitive market in the grocery sector, from which the competition tests can then be derived. In effect, the Commission would be testing the merger against the desired future state for the grocery sector – a competitive market – not the likely future state of the continuance of the duopoly.

And using these new criteria is highly likely to result in the merger being declined.

We do not think it is likely that the Commission will pursue this option, for the following reasons:

1. As noted above, there is little evidence the Commission has the conceptual frameworks or the policy structures to directly address failed markets. In our view, a failed market is an Outside Context Problem for the Commission, which means it has trouble seeing the duopoly for what it is and then responding appropriately. Expecting the organisation to overcome the cognitive blocks and act with alacrity in the context of the merger application is probably asking the Commission to travel too far, too fast.

2. Setting out new assessment criteria based on the wider objective of restoring competition to the grocery sector will be seen as risky by officials. Given the excessive caution of all Crown agencies, it seems unlikely that the Commission would be prepared to proceed with new criteria without an extended period of hand-wringing. This will probably place the process well outside the timelines for assessment of the Application, particularly in light of the fact it took the organisation some 17 working days to merely compile the SOPI.

3. As a result, there is a high likelihood the Commission, its process and its criteria would be subject to legal challenge from Foodstuffs, something which officials seem inordinately concerned about. And unlike Option 2, the Commission would have little leverage to incentivise Foodstuffs to withdraw the application.

In our view, this Option has considerable merit – primarily because it provides a way of developing the conceptual frameworks and policy tools to enable other oligopolies – such as in banking, electricity, building products and other markets – to be unwound in the future.

We also note that there is a pathway open to the Commission to test and validate the use of alternative assessment criteria – notably, the courts.

Assuming the Commission elected to use different criteria, it could reasonably expect a legal challenge from Foodstuffs – and in our view, this is no bad thing. Seeking clarification from the judiciary on the extent and limits of the Commission's assessment powers would prove beneficial to not only the Foodstuffs merger, but to every other consideration of acquisitions and mergers where there is evidence of market dysfunction. The organisation's track record of not troubling the courts on competition matters is troubling, and is not taking the country in a useful direction.

And addressing the resulting problems is a pressing need. The Commission's poor decision making over the last two decades has led to invidious outcomes for individuals, businesses and the wider economy. It's past time for the Commission to stop approving mergers and acquisitions that are clearly not in the national interest, and to do so it needs better approaches and tools. Unfortunately, there is little evidence the organisation has even commenced this journey.

The strategic context

As noted, we think it most likely that the Commission will adopt Option 1 and approve the merger. In doing so it will be travelling a well-worn path of prioritising process over outcome, and will fail to acknowledge that a merged Foodstuffs entity is not in our national interest.

Taking this course of action is entirely defensible for officials. However, approval brings with it a very significant risk: that it will provide endorsement to allow Aotearoa's oligopolies to act with impunity when it comes to mergers.

The implications are best explored as a thought experiment. Assuming the Commission approves the Foodstuffs merger on the basis that it will have little discernible impact on competition because of market failure, what is to prevent Foodstuffs and Woolworths putting forward a merger application? After all, if there is already negligible competition in the grocery sector – as the market study states – then why would it matter if there is a duopoly or a monopoly? After all, the adverse effects on consumers will be identical.

Bearing in mind the elegant arguments put forward by the Chapman Tripp team in this application, it is safe to assume an equally coherent and internally consistent argument could be put forward for a full monopoly. And these arguments will travel just as well for the banking or electricity or building products markets – in fact, anywhere there is strong evidence of market failure.

Further exploring the thought experiment, Westpac Bank has indicated it wishes to sell its New Zealand business. If the Foodstuffs merger is approved, then there is a strong argument that any of the other Australian banks can be the acquirer of Westpac, as the market failure in the banking sector will be fundamentally unaltered.

The Commission appears to be on very slippery ground indeed.

The preferred option

As noted, the Commission's track record indicates it will choose Option 1 and approve the merger – even though it runs a very significant strategic risk in doing so.

However, if we look at the options through the lenses of Effectiveness and Achievability, it is apparent that Option 2 is the preferred option. This is because:

- **The option will be effective**. It will observe the current procedural approach, is unlikely to face legal challenge from the applicant and will result in the desired outcome – that is, either Foodstuffs withdrawing the application or facing court for the abuse of market power (preferably both).
- **The option is achievable.** It does not require additional policy development or legislative change, as the tools and the public mandate are all available to the Commission today. And presumably, within the 400-strong army of staff employed in the organisation, the resources are available to commence action against Foodstuffs under s36 of the Commerce Act.

There are impediments, which are entirely of the Commission's own making. It has little track record of major prosecutions nor the apparent intestinal fortitude to undertake the process, which will undermine the credibility of the threat of court action. And it may feel that it has insufficient political support, even though every political party in the country has expressed concern about the cost of groceries and the cost of living, and every person standing in the supermarket checkout lines will be cheering in support. This will not prevent the Commission continuing to be frightened by the slightest opposition.

Importantly, however, the Commission has the moral responsibility to act, and in doing so, restore its very diminished mana.

You broke it, you fix it

The market failure in the grocery sector and the resulting duopoly is the direct responsibility of the Commerce Commission.

The current state of affairs has not arisen because of an Act of God or the intervention of some *deux ex machina*; it is the direct and attributable result of the Commission's acts and omissions over the past two decades. Had the Commission not approved mergers and acquisitions, and then stood idly by whilst market power was consolidated and then abused, every whānau in the country would be paying less for groceries than they are today.

Concerningly, the market study offered no analysis to why excessive consolidation in the sector had occurred, so there was clearly little self-reflection from the Commission as to its sometimes complicity with and sometimes active encouragement of the market failure in the grocery sector.

Accordingly, it is up to the Commission to set this to rights, and it is time to end the magical thinking that says some bureaucratic fiddling in the margins and some voluntary codes of practice are going to result in structural reform and the return of competition. In the nearly two years since the release of the market study, there is scant evidence of lower prices, the level of competition has likely decreased, and the level of profitability of the duopoly remains substantially unchanged.

The Commission will undoubtedly point to the new legislation and the freshly-minted Grocery Commissioner and state that more time is needed, but at the current rate of excess profitability, the only result from more time will be the continued impoverishment of whānau, with little end in sight. Process is no substitute for outcome.

Which is why we are very much of the view that Option 2 – the approval of the merger, along with the s36 prosecution of Foodstuffs for its historical and ongoing abuse of market power – is the right way forward. This approach is both effective and achievable, and we strongly recommend it to the Commission.

Endnotes

1 Commerce Commission. (2022). 'Mergers and acquisitions guidelines', retrieved https://comcom.govt.nz/__data/assets/pdf_file/0020/91019/Mergers-and-acquisitions-Guidelines-May-2022.pdf

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