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2 **DAY 5 - RETAIL GROCERY MARKET STUDY CONFERENCE**

3 **28 October 2021**

4 **Session 7: Options to improve conditions for entry and expansion**
5 **Session 8: Options to improve conditions for entry and expansion – wholesale**

6
7 **Ms Rawlings:** Morena, tēnā koutou everybody, welcome back to another day of our conference
8 into the grocery market study. Welcome back for those that have been with us all week
9 and welcome to those who are joining us for the first time today and I think there are, at
10 least, a couple. Ko Anna Rawlings taku ingoa, I'm Anna Rawlings, the Chair of the
11 Commerce Commission and with me for the conference are Commissioners who have
12 been working on the market study. They are Dr John Small, Dr Derek Johnston and Vhari
13 McWha, Associate Commissioner. We also have with us a number of staff who have been
14 working on the study as well.

15 As you know, the purpose of our market study has been to look at factors affecting
16 competition in the market for the supply or acquisition of groceries in NZ and to make
17 recommendations that we think could improve competition if those are necessary and if
18 we think that it's not working as well as it could. Our draft report set out our preliminary
19 findings in relation to those matters and both the conference and your comments are
20 providing some important insight that will assist us to reach our final conclusions for our
21 final report.

22 The conference provides an opportunity for new issues to be raised and for issues
23 that have already been raised, to be discussed in a bit more detail with some greater
24 focus. It's also enabled parties to hear a little bit more from one another and to
25 understand better the positions of other parties.

26 Today's sessions are going to cover matters relating to barriers to entry and
27 expansion and we're going to begin our discussion about options for improving conditions
28 for entry and expansion. We're going to run this morning's session until 10.45 and then
29 we'll take a break as we have on other days to 11.15, pick up again and schedule to finish
30 at about 12.30 today. We'll then work through the remaining issues on our agenda and
31 just one designated day to go on Monday, no session tomorrow, but by the end of the
32 week we'll let you know whether we think that we need the session on Tuesday, which
33 has been set aside with no allocated topic at this point.

34 I want to reiterate again that the conference isn't the last opportunity for parties
35 to have their say on our draft report or on the market study more generally. We have
36 invited further comment through submission on matters that are raised by others and
37 raised at the conference and those submissions are due by the 23rd of November. We
38 might also follow-up with some more specific questions for those who have attended the
39 conference, but also for those that haven't been heard at the conference. And you'll hear
40 from us if that's the case for you.

1 In addition, I just want to reiterate some comments I made at the beginning of the
2 conference and that is that we have read all the submissions that have been provided to
3 us in relation to our draft report and we've heard some very useful broad range in
4 introductory comments to some of the sessions so far in the conference. I think the
5 essential draft findings of the Commission are well known and have been well discussed
6 and the positions of major participants in the study also are fairly well known and have
7 been clearly set out for us.

8 We've moved away from the use of introductory comments for every session
9 because it will just provide us with a greater amount of time to prioritise discussion and
10 question time for those issues arising where we're looking for clarification, or we consider
11 that some dynamic discussion between parties will help us to eliminate the issues. And
12 it's that dynamic discussion which is most useful to us at this point in progressing our
13 thinking.

14 So by all means, as you're presenting to the conference, please do point us to
15 places in your written submissions where we might find additional information, but we
16 don't need submissions repeated in the course of conference for the conference record,
17 we really just want everyone to focus on the issues identified by the Commission for
18 further discussion and illumination rather than presentation on matters that we have in
19 submissions. And I'll reiterate again, that there is that opportunity to provide us with
20 written comments or further notes after the conference.

21 Now just to reiterate some housekeeping matters, particularly for those joining us
22 for the first time. If there's documents that you're referring to for the first time in the
23 conference sessions, please do remember to send them through to us either at our email
24 address, marketstudies@comcom.govt.nz or with your further submission by the 23rd of
25 November. If you've got any questions during the course of the sessions or the
26 conference, you can also use that email address to contact our team and they'll come
27 back to you as soon as they can.

28 As has been the case so far, the session will be chaired by one of the
29 Commissioners and we ask that the discussion is facilitated through the Chair so that we
30 can keep an orderly discussion going. As you can see it's run in a webinar format for those
31 joining us for the first time and that means that if you indicated that you'd like to
32 participate in the session, then you will have been joined to the webinar as a panellist and
33 you'll have the opportunity to directly and immediately contribute to the discussion when
34 invited to without taking any further steps, other than of course, unmuting your
35 microphone please and turning your camera on. And we ask when you're not speaking if
36 you can also ensure that your microphone is muted, at least, and up to you whether you
37 keep your camera on, but muting microphones is important to avoid a feedback loop in
38 particular and background noise so others can hear clearly.

39 If you could also, when you speak for the first time in the conference, just let us
40 know your name and organisation so that our transcriber can pick that up easily during
41 the transcription service.

1 If you've indicated that you wanted to attend in an observer capacity only, then
2 you will have been joined to the webinar as an attendee and we don't want that to
3 prevent you though from contributing to discussion if you'd like. So if there's something
4 that you'd like to comment on and you're attending in the attendee group, please raise
5 your hand using the Zoom function and a member of our team will contact you and enable
6 you to join the panel so that you can also contribute if you wish.

7 For reasons like time or technology that doesn't prove possible, and there's
8 something that you want to add that you haven't had the opportunity to add, then please,
9 again, I emphasise, follow-up with written submissions or with further discussion with our
10 team after the conference, we really want to hear everything that everyone has to say.

11 We can also say for private discussion anything that you'd like to contribute which
12 you consider to be confidential or commercially sensitive and if something arises in the
13 course of questioning which you'd rather not talk about openly in a public forum, please
14 just let us know and we can defer that for a later time.

15 You'll note from the live feed that the conference is being recorded, that's solely
16 for the purpose of our transcription service and we'll provide a transcript of the
17 conference on our website as soon as we can, we don't intend to make the recording of
18 the conference available to parties. And on that note too, just a reminder that we have
19 welcomed media to the conference who will come and go as they choose, but we've also
20 asked that media don't record the conference either.

21 Thanks very much for that, I'm going to hand over now to Vhari McWha and she's
22 going to lead this session for today.

23 **Ms McWha:** Morena koutou. In this session we'll be discussing our draft findings and options
24 relating to conditions of entry and expansion. We've heard from the major supermarkets
25 that they compete for shopping trips with a range of different retailers and that the
26 combination of these often relatively small retailers, is a constraint on them. However,
27 we've heard from retailers wanting to expand or enter that there are a number of things
28 stopping them from doing so and that this constrains their ability to compete.

29 Our preliminary view outlined in our draft report was that some conditions of
30 entry and expansion may hinder the ability of grocery retailers to enter and or expand to a
31 scale to directly compete with the major grocery retailers. Over the next couple of
32 sessions, we will talk about some of the factors that we think are likely to be preventing or
33 slowing entry and expansion in the retail grocery sector and the options for alleviating
34 them.

35 I wanted to briefly mention terminology. If I refer only to potential entrants, I do
36 also mean a retailer who would like to expand. Expansion can take the form of expansion
37 of product range, or geographic location, or expansion from another sector such as
38 general merchandising, or expanding into a different part of the supply chain.

39 The Court has referred to the threat of entry as the ultimate regulator of
40 competitive conduct and as such, the ease with which firms may enter or expand, is very
41 important to our conclusions and recommendations.

1 In this morning's session, we're planning to discuss the need for scale, access to
2 infrastructure, access to capital, and the availability of sites. We will talk more about
3 access to wholesale supply after the morning break. There's a lot to get through this
4 morning and while we have some flexibility to come back to these topics later if we need
5 to, I have Ben Hamlin, our Chief Legal Counsel sitting next to me and I've asked him to
6 help me keep things on track if we need to. If we do not get to cover everything you
7 would like to tell us, as Anna has already explained, or if you think of additional material
8 later that you would think would be useful, then please do send it through to us at our
9 email address, marketstudies@comcom.govt.nz by the 23rd of November.

10 Let's get started.

11 So, our first topic relates to the particular characteristics that are required of a
12 retailer for it to be an effective competitor with the major retailers. There are different
13 market conditions that can affect different types of retailers in different ways. For
14 example, the availability of sites might be more relevant as a condition of entry for larger
15 bricks and mortar retailers than those with a smaller footprint, or those who have an
16 online only presence. Because of these likely differences and one of the most important
17 conditions for entry and expansion, I'd like us to talk briefly first about what an effective
18 competitor looks like.

19 Now, we've already mentioned that the major retailers have told us that they can
20 consider that many of the existing retailers and what we described in the draft report as
21 "the fringe", are competitive constraints. However, as we noted in our draft report, these
22 fringe competitors do not generally compete on all aspects of PQRS (price, quality, range
23 and service) and are not usually seen as a substitute for a main shop for a household.
24 They also do not generally have the same geographic reach as the majors.

25 Following our discussion last week about the nature of competition, it seems that
26 the position as a main store with a comprehensive range, is an important competitive
27 advantage across all shopping trips or missions.

28 So with that background, I'd like to first ask the smaller retailers and potential
29 entrants about what characteristics they consider are required of a retailer to be able to
30 compete effectively and profitably with the major retailers.

31 I wondered whether Sarah Balle from Supie might like to speak to this point and
32 Sarah, whether you consider that there's a minimum scale needed to compete effectively
33 with the majors in terms of store size or number of stores?

34 **Ms Balle:** Hi everyone, I'm Sarah Balle from Supie and I just want to touch on the point around
35 scale. So, it is without a doubt, in our view, that you need scale to be in an effective
36 competitor with the major retailers. And this is scale in two areas.

37 The first is to scale sufficiently to receive competitive pricing from suppliers, which
38 I know will be discussed in the next session on wholesale supply.

39 But secondly you need sufficient scale to be a viable business. This, and in
40 particular for Supie as a main shop operator, we need scale to cover our fixed operating

1 costs, technology and development costs, marketing and infrastructure costs. And what
2 Woolworths NZ turns over in an hour is what we do in 6-months. Supie has been
3 mentioned several times throughout the conference already, yet we do not currently have
4 sufficient scale to be considered an effective competitor. And I'm happy to discuss soon
5 when we touch on capital requirements because this is what we need to support scaling
6 to be effective.

7 **Ms McWha:** Sarah, do you think that there's a minimum geographic reach that is required?

8 **Ms Balle:** Not necessarily. As an Auckland based operator currently, it would be scale within
9 certain geographical areas, but for us at Supie, we're looking to go nationwide, but we
10 need scale to assist us in doing that and that will be part of our capital requirements kind
11 of conversation as well.

12 **Ms McWha:** Thank you. You touched on the need for scale in order to be able to access
13 competitive prices from suppliers, so I wondered if you wanted to also comment on
14 whether it's necessary to be vertically integrated to be able to kind of achieve scale, or
15 whether it's possible to do that without that vertical integration? When I say vertically
16 integrated, I mean with the wholesale part.

17 **Ms Balle:** Yeah, so at Supie we're currently vertically integrated, but in our view, access to
18 wholesale products is absolutely necessary and the current offerings of wholesale supply, I
19 think Gilmours and BidFood have been mentioned, that's simply not viable and that's not
20 just in terms of cost, but the range of their product offerings and getting sufficient and
21 consistent supply from them. And that's why we have spent more than 2-years
22 developing our own access to wholesale supply at great investment. And we want to see
23 regulatory intervention as a step in the right direction and that will break down at least
24 one of the barriers to entry and barriers to scaling in competition.

25 For Supie, that's not necessarily in terms of physical infrastructure of wholesale
26 supply. But in terms of access to suppliers' product range and that competitive pricing
27 that the duopoly receive.

28 **Ms McWha:** Thank you. Do you think there's any specific differences or that are important as
29 between yourself as an online only retailer and a bricks and mortar retailer that we should
30 be aware of, in terms of the conditions for entry?

31 **Ms Balle:** Yeah, I'm unsure on bricks and mortar, and others can probably respond to that, but in
32 terms of online only, I've kind of touched on the points that we require, that scaling
33 wholesale and access to capital which is one of the next topics I think.

34 **Ms McWha:** Yep okay, thank you. I'm not sure if we've got Matthew Lane online with us this
35 morning, Matthew did you want to comment on scale in terms of being an effective
36 competitor and what the scale requirements are?

37 **Mr Lane:** Yeah good morning, Matthew Lane, Night 'n Day. Look just to sort of reiterate some of
38 the points there. I think the problem is around the scale that you need. It's not
39 necessarily reaching a certain level of scale within the market, but it's the actual gap
40 between the current players in the market and then the next tier down.

1 If you looked at a competitive markets have a range of competitors, certainly
2 increases competition and it increases diversification in the overall buying power they can
3 attract.

4 For us the gap between buying power as our brand compared to Foodstuffs or
5 Woolworths, is so significant it becomes hard to bridge that gap regardless what scale you
6 have, they're always going to hold a significant amount of greater power and for us to try
7 and compete in that bricks and mortar space, right the way across NZ, becomes hard for
8 us to scale up in terms of that medium format store. Both brands have that medium
9 format store currently as they can leverage the buying power to make them a lot more
10 economical, but it's hard to organically grow from a smaller format to a medium format to
11 a large format in NZ because ultimately you're relying on the wholesale network of
12 Woolworths or Foodstuffs.

13 That wholesale network, certainly from a Foodstuffs end, is incredibly
14 uneconomical and prevents the ability to grow into that space and by having the two main
15 wholesale aspects available to us, being direct competitors, gives insights and advantages
16 that you wouldn't expect in the competitive market and I guess that reduces the want to
17 invest in this area and grow that area because you're solely reliant on, I guess, the
18 goodwill in some respects, of these companies to supply us the products that we need to
19 be able to invest and grow the retail side.

20 **Ms McWha:** Thanks Matthew. I wondered if you would be able to comment on some of the
21 factors that you consider when you're deciding whether to open a store in an area,
22 because I think that will help us to think about what the conditions for entry might be?

23 **Mr Lane:** Yes, certainly we look at competition in the nearby area. We do look at population size.
24 At this stage we find ourselves very good in the rural sectors, whether there is a lack of the
25 dominance from the major retailers and we tend to act a lot more of that medium size
26 shop more so than anything else. But yeah, there's a whole range of factors that we do
27 take into consideration, to isolate one or two would be hard. But certainly foot traffic is a
28 major part of what we do, but we do operate in CBD locations, suburban location, rural
29 location. So certainly nothing excludes us from being in there, probably what does
30 determine a lot of our outcome is the size of retail premise we invest in at the moment
31 because there's only limited return on investment that we get out of that grocery space
32 with the buying power we have and our competitiveness in it.

33 **Ms McWha:** Okay, thank you. Perhaps Northelia, is there anything that you would like to add on
34 this issue of scale in terms of entry?

35 **Mr Botica:** Tēnā koutou katoa. Ko Allan Botica taku ingoa, ko Botica Butler Raudon Partners te
36 umanga. I don't want to talk about scale. I do have a statement from Northelia if the
37 Commission would like me to read it now?

38 **Ms McWha:** I wonder, just as Anna mentioned earlier, we are a bit short on time –

39 **Mr Botica:** So we'll defer then, yeah?

40 **Ms McWha:** Yes or you might send that through to us if that's okay Allan, that would be great.

1 **Mr Botica:** Cool, will do that.

2 **Ms McWha:** Thank you. Tex, did you have something that you wanted to say on the question of
3 scale?

4 **Mr Edwards:** Yes, Monopoly Watch in conjunction with Northelia has done a lot of work on scale.
5 We think the concept here and I applaud my industry colleagues, Sarah and Matthew's
6 comments, we need a third supply chain facility because both of those organisations are
7 currently, in their business cases, would be reliant on the incumbents.

8 At the scale level, we think an entry of approximately 15% market share at around
9 \$3.5b in the 22-billion-dollar industry is sensible. We think circa 150 stores with the
10 current ecosystem of 450 stores covering Auckland, Wellington, Christchurch, Dunedin,
11 Tauranga, Hamilton, to start off with, and then a general expansion into provincial NZ
12 where 87% of NZ's population is urbanised, and we see the scale issues as absolutely
13 essential because although it's a highly profitable industry in NZ, there's still a low margin
14 industry.

15 It's a low margin industry with capital intensity. And so a challenger is going to be
16 a hybrid challenger Commissioner. We're going to see a combination of internet
17 initiatives, bricks and mortar initiatives and also if I could just allude to Commissioner Sue
18 Begg's letter of March of this year, some of the competing factors on the challenger are
19 actually going to be carbon footprint, sustainability and a third operator challenger will be
20 competing in a 2023 context, not a 1993 context.

21 So I urge the Commission to look at those possibly changed metrics and just share
22 my inspiration from Commissioner Sue Begg's letter of March of this year.

23 In summary, the biggest cost, the biggest cost for a challenger when we modelled
24 it in conjunction with the Northelia Board, is actually the J-curve and the operating losses
25 in the first 3 to 4-years, that's the hell-zone period for a start-up, and my experience in
26 this matter is that we're going to see a vigorous, almost violent reaction from incumbents.
27 Pricing is not going up, I mean, please, pricing is coming down and we summarise our
28 point in saying we're going to be operating in a lower margin less profitable industry and
29 so the actual store dynamics, the store dynamics in suburban stores, they're going to be
30 less profitable because margins are going to come down.

31 So we urge the Commission to think through that when they're discussing scale.
32 Thank you.

33 **Ms McWha:** Thank you. Foodstuffs or Woolworths, I wonder if either of you would like to
34 comment on what you've heard so far? Josh, I see you have your hand up, thank you.

35 **Mr Gluckman:** Thank you Commissioner, morena, kia ora koutou katoa, ko Josh Gluckman aho,
36 no Woolworths New Zealand aho. Josh Gluckman from Woolworths NZ. I'll touch briefly,
37 Commissioner, on both scale and vertical integration in the interests of time and I won't
38 cover all of the territory that we've included in our submission for all of the reasons
39 outlined in the introduction.

1 Our view is that we don't think that there's a minimum scale or a prerequisite
2 model that exists in order to be an effective competitor in the NZ marketplace. As we've
3 already noted, we observe and we face and we experience already, rapidly increasing
4 competition on lots of different dimensions, right, whether that's convenience, whether
5 that's online, whether that's pricing, or more, and of course competition comes in lots of
6 different shapes and sizes. And so, you know, certainly for us it is the case that our scale
7 and our vertical integration deliver a number of significant benefits. And those scale
8 benefits are important because they translate to efficiencies, end to end, throughout our
9 supply chain that are passed on to Kiwis and customers in terms of lower prices and lower
10 costs.

11 And so our business model is highly sensitive to scale. Our unit costs are highly
12 sensitive to scale as we've outlined in our submission. Whether that's our supply chain,
13 our IT, our buying, our management structures, our systems, our online capabilities or
14 analytics. Our unit costs go up if our scale is impacted and it doesn't take much to
15 increase those unit costs and that's unlikely to be a good thing for Kiwis, in our view it
16 would be a recipe for higher prices, not lower. So you'd certainly want to preserve the
17 benefits of our scale.

18 Similarly vertical integration delivers a ton of benefits. Obviously I won't rattle
19 them all off, but you know, a much smoother flow of goods end to end, across the value
20 chain, reduced double marginalisation. Much more effective and integrated forecasting
21 efficiencies and the ability to manage products through to the shelf. A lot of improved
22 end to end efficiencies and quality control, whether that's farm to fork with things like
23 shelf-ready cases and trays that we could work with our suppliers to work right through
24 onto the shapes of our shelves.

25 And of course managing crises, which we might come back to later on over the
26 course of today or early next week where we think a separated or a wholesale model
27 would have a number of significant issues.

28 And so, you know, we do think its important that the benefits of our scale and
29 vertical integration are preserved and that's why we're not supportive of the number of
30 some of the more extreme options that have been entertained.

31 And if we think about what shape and size market entry might entail, you know,
32 again, we already see it in a number of different shapes and sizes. Typically we think it's
33 likely to start small and then scale and that is what we see and what we are seeing. You
34 know, it might be a Costco with a one store albeit a stated intent to open three, and
35 obviously those three stores would still be equivalent to 18 Countdown stores in terms of
36 their size and those three stores would have 40% of NZ's population within their 25k
37 destination radius before online.

38 Chemist Warehouse started small, quickly scaled, now 25, on their way to 70
39 stores. Farro have now scaled, \$100m. Meal kits, Hello Fresh, My Food Bag have quickly
40 scaled \$400m. Aldi in Australia we expect, you know, when they enter here, would likely
41 scale quickly, they open 25 stores per annum over a sustained period of time.

1 So we think entry is likely to take the shape of starting small and scaling. And in
2 the case of Costco of course, global scale.

3 **Ms McWha:** Thanks Josh, appreciate that. I see that Matthew and Sarah have their hands up, so
4 Matthew perhaps I could come to you.

5 **Mr Lane:** Yes, thank you. I just wanted to touch on a point that Tex made around violent
6 reaction from the incumbents with any new competitor coming in. I just want to touch on
7 an example that we sort of experienced first-hand and have since sort of burnt our, I
8 guess, willingness to continue around the dry grocery on the scale that we'd previously
9 operated on.

10 Back at about 11 or 12-years ago we expanded to the North Island. We added 21
11 stores to our network. They were previously Woolworths Quick Stop stores and had a
12 very strong grocery and top-up shop associated with them. Now, we had access to
13 grocery wholesale on the same terms as the members, from Foodstuffs SI, and that gave
14 us the ability to be competitive in the dry grocery space.

15 Now, when we were expanding to the North Island and added those 21 stores, we
16 expected to be able to maintain and hold some of those sales that had been previously
17 built up by Woolworths NZ. But within 6-months, we'd actually had our membership
18 revoked and had no ability to be able to obtain any form of supply that could prove
19 competitive in that market. And as a result, that main sort of dry grocery top-up shop,
20 baby food, etc, evaporated from those stores and has relied more on coffee and milk bar,
21 your food-to-go aspects of it.

22 So I certainly am very cautious around the reactions from the incumbents with any
23 form of growth in the market and I do reiterate Tex's comments that it would be highly
24 likely that any form of competitor entering that market, would face strong reactions to the
25 new competitiveness of it.

26 **Ms McWha:** Thanks Matthew. Sarah.

27 **Ms Balle:** So I guess one point that I'd like to make is that everything that Josh Gluckman from
28 Woolworths NZ has said demonstrates all of the elements that a new entrant has to
29 create in order to enter the market and this is a complete barrier to entry. And his point
30 around Farro being \$100m turnover business, that's not an effective competitor. That's
31 not even 1% market share.

32 **Ms McWha:** Thank you Sarah. Chris Quin from Foodstuffs NI.

33 **Mr Quin:** Thank you Commissioner McWha. Look, just to add Foodstuffs' view on the key
34 questions around minimum scale and access to the scale as briefly as I can.

35 I think the first concern I would have is that there is a bit of an underlying
36 assumption that the only way to compete in the future will be to do exactly the same
37 thing as the incumbents. And I think a few points have been made that say, actually it is
38 very likely, as with almost every industry that future competition will bring different and
39 alternative offers and business models to market.

1 We see current competitors, and it's been well displayed this morning, come in all
2 shapes and sizes, including large, medium, and small retailers, and they'll compete
3 nationally or locally for the shopping missions which has been well discussed.

4 We think that even entrants that compete across the full range may well adopt a
5 disruptive or different business model to ours. So, Aldi has a very different business
6 model. Supie has a very different business model, that is the future of competition in
7 every market including this market.

8 Retailers like Chemist Warehouse, The Warehouse and soon Costco with multiple
9 stores, will be major retailers for particular grocery items on a nationwide basis. And I
10 note that Warehouse Group's fastest growing category in their recent results was dry
11 grocery. But equally small retailers, such as local green grocers, butchers, fishmonger
12 compete with us and compete often on price and non-price dimensions and we see it
13 every week.

14 So we think the future of competition will be a mix of niche and very capable and
15 very targeted offers. And we genuinely do see every week new competing offers come
16 and they compete on price, on quality, on range and on service.

17 So, we face price competition in almost every mission, as discussed before, and
18 need to try and compete in almost every mission. You know, classic example, most of our
19 stores would be looking at their local Fruit World regularly and considering their produce
20 pricing department on a weekly basis.

21 There is no doubt you can't deny volume results in price advantages and
22 economies of scale and volume discounts are common features in almost any retail sector
23 and consumers benefit from that and we've proven through the data share, the pass-
24 through does exist and does occur.

25 So, scale advantages are demonstratively not necessary to compete effectively
26 existing grocery retailers, we're likely to see the competition emerge in very different
27 ways. And there are different ways to offer lower prices so the different hybrid models in
28 the futures will have significantly lower overhead costs. It's been mentioned that this is a
29 low margin/high capital industry, future models will try and adjust the capital piece in
30 particular to try and make it more economic.

31 And price is not the only dimension that we see competition in. Joint buying is
32 already the subject of a Commerce Act exemption, so retailer buying groups may well be
33 part of the future that occurs in order for advantage to be gained.

34 So in terms of our view is we are seeing active arrival of competition in the current
35 market with different business models.

36 **Ms McWha:** Thank you. Now I'm just conscious of time, I see Tim Donaldson for Foodstuffs SI
37 has his hands up, I wonder if you could briefly comment on this Tim.

38 **Mr Donaldson:** Thank you Commissioner, I'll be very brief, but before I start, I'd just like to
39 respond to a comment that was made and I can't go into the details and won't go into the

1 details of why Night 'n Day were removed from membership from Foodstuffs SI. Having
2 said that, Night 'n Day did complain to the Commission and the Commission found in our
3 favour, so I just wanted to make that point.

4 **Ms McWha:** Okay, thank you.

5 **Mr Donaldson:** But we don't believe that it is a question of scale. If you have a good offer that
6 meets the needs of the customer across all these aspects of PQRS, then you can compete
7 effectively with major retailers. And as we've already detailed, there are numerous
8 examples in the South Island of retailers competing with us. For example, Night 'n Day
9 have grown from one store in Dunedin to 50 stores nationwide. And among others, the
10 Chemist Warehouse, Animates and The Warehouse also compete aggressively with us
11 across numerous categories and aspects of PQRS. Thank you.

12 **Ms McWha:** Okay, thank you Tim. Andy Matthews, did you have a comment?

13 **Mr Matthews:** Yes I did today, it's a bit hard to know where to begin because quite a lot has
14 been thrown in there once again.

15 I think the question was about scale and first of all, we were told there were no
16 scale advantages and then we were told there were high economies of scale and benefits
17 of vertical integration, which can't be touched, which almost sounds a bit like suggesting
18 the minimum efficient scale is only two. And then, once again, we're sort of jumping in to
19 suggesting that non-grocery retailers are substitutes for the full shop. So it's a bit hard to
20 know where to begin.

21 But I think it's more a question of saying, what would the model be to provide the
22 same bundle? And I think my concern with what we are hearing is that we're getting a
23 bunch of different things thrown in together and yet again we still haven't shown that
24 there is any substitutability or constraint or levels of cross-elasticity of demand. So non-
25 grocery shops are being compared to grocery shops. And I think Nick from Quadrant,
26 made the point, Hexis Quadrant, made the point that in many cases this could actually
27 show growth of supermarkets into other areas.

28 But it does seem that there are economies of scale and that seems clear. So I think
29 the question is really more, is it suggested that the minimum efficient scale for NZ is so
30 large, such that NZ can support only two full-scale grocery retailers? And that probably
31 seems to be the issue to drill down in.

32 **Ms McWha:** Thank you Andy. Tex, I see you waving there, do you have one very quick comment
33 before I move on?

34 **Mr Edwards:** Absolutely Commissioner, just one sentence, just one sentence. The sentence
35 comes from the telecommunication industry in NZ. The sentence is, if you have scale, it
36 doesn't matter what technology platform arises, if you've got scale you can transfer it
37 from one technology platform to another. Thank you Commissioner.

38 **Ms McWha:** Thank you. So I would like to move on now to our second topic which relates to
39 issues surrounding access to supply chain infrastructure.

1 So we heard from some potential entrants that access to infrastructure is a
2 significant issue that limits their ability to compete effectively. In their response to our
3 preliminary issues paper, Foodstuffs noted that access to temperature-controlled supply
4 chain infrastructure could affect entry.

5 In contrast, Woolworths indicated that they rely on third-party logistics providers
6 at times to provide warehousing and transport, and they've said that they do not consider
7 that logistics networks are a barrier to entry.

8 So we would just like to try and clarify whether there is an issue here, specifically,
9 around supply chain infrastructure.

10 So first of all if I could ask the majors if possible, to comment on their current
11 strategies in terms of vertical integration into the supply structure, so we're interested in
12 thinking about, I guess, in particular, Foodstuffs, if you could explain whether you
13 currently use third-party supply chain providers and what the advantages are from your
14 perspective of the approach that you adopt. Chris, is this something that you are able to
15 comment on?

16 **Mr Quin:** Thank you Commissioner, yes I can. So look, I'm not sure if vertical integration is the
17 right term, but essentially, we are a business that buys product and then supplies it
18 through a supply chain that we recover the cost of to our stores to put the range on shelf
19 for customers. And I think it's important that, like many retailers in NZ, we supply direct
20 with suppliers going direct to our stores as well as through our supply chain. And the
21 simple definition or the deciding factor when we do that is what provides the best quality
22 and cost mix from the point of view of the customer outcome.

23 To give you an idea we range about 80,000 products, only about a quarter of those
24 go through our own supply chain. The rest of it is more efficient for it to go direct from
25 the supplier to the store. And we simply do our best to make sure that we put that
26 through.

27 **Ms McWha:** Sorry, can I just understand then, with the things that are going directly to your
28 store, the delivery is the responsibility of the supplier?

29 **Mr Quin:** Or a third-party they had contracted to do that, which is quite common. So if I then
30 relate it to chilled and frozen was mentioned in particular, I believe our submission
31 pointed out that our capacity within our own business was starting to reach the point of
32 full capacity. And that we need to consider further investment into that. We are already
33 using some third-party arrangements for capacity in that market. And we would make the
34 point that in general, 3PL capacity for supply chain and logistics is available in NZ market
35 and is a solution that can support entrants and is being used by many.

36 **Ms McWha:** Okay, so from your point of view then would you consider that supply chain
37 infrastructure was a significant part of the investment to enter the retail grocery market?
38 Or it sounds like it's perhaps not so important.

39 **Mr Quin:** It's our view and experience that it is available to entrants to consume as a service
40 from partners and that there is capacity in NZ to do that.

1 **Ms McWha:** Okay, thank you Chris. Tim, did you want to add to that from the South Island
2 perspective?

3 **Mr Donaldson:** Thank you Commissioner. We don't believe that supply chain infrastructure is a
4 limiting factor. There are numerous options for both warehousing and distribution in the
5 South Island. And in fact we utilise ourselves third-party warehousing and transport
6 providers regularly, as do many of our suppliers.

7 It's important to note that more than 40% of the transport that we use is from
8 third-party suppliers. And just following up on a point that Chris raised, 49% of our
9 products go direct to store from suppliers.

10 **Ms McWha:** Thanks Tim. Does that comment you said, 40% is third-party suppliers, is a
11 proportion of that chilled or temperature controlled?

12 **Mr Donaldson:** No, temperature controlled, we do on our own network. So the majority of that
13 would be ambient.

14 **Ms McWha:** Okay. And are there third-party options available for chilled?

15 **Mr Donaldson:** Absolutely, yeah, so a number of our suppliers will be using third-party for chilled
16 distribution throughout the South Island.

17 **Ms McWha:** Okay, thank you. Woolworths, Josh, do you have any comment on our approach to,
18 I'm particularly interested in chilled, because that seemed to be where the issue was
19 being raised?

20 **Mr Gluckman:** I'll keep it very brief. We similarly observed that there are third-party options
21 available. We use third-party options extensively throughout our supply chain, so we
22 lease our DC sites from third parties. We've got transport and logistics contracts with
23 third parties and we use Americold as our third-party for chilled. And we also note that
24 they have some capacity to support others and so we observe that there are options
25 there, so we don't think that those capabilities are likely to be beyond reach for others.
26 Thank you.

27 **Ms McWha:** Okay, thank you. I wonder if any of the entrants would like to comment on this,
28 Tex, I see you have your hand up.

29 **Mr Edwards:** One sentence again Commissioner. The industry rule is like for like infrastructure,
30 like for like competition, and it's the like for like infrastructure, only the paranoid survive
31 as challengers. So if you have A, B and C correct and your business is humming along,
32 you're burning tens of millions dollars a month, it's the gorilla in the ambiguity, it's the
33 item that you don't have that's going to blow your business and our point here is like for
34 like, thank you.

35 **Ms McWha:** Thanks Tex. Supie, I'm aware that you didn't have any specific concerns I don't
36 think, when you mentioned your concerns earlier, you didn't mention access to
37 infrastructure, just wanted to make sure that nobody else wanted to comment on that
38 point at this stage? Okay, thank you I'll move on then to access to capital.

1 So, access to capital has also been raised as a factor. I'd like to focus first on
2 domestic capital before turning to the Overseas Investment Act and what regulatory or
3 other barriers there might be to accessing international capital.

4 So Sarah, from Supie, perhaps if I could come to you first. You've raised that
5 capital is a significant constraint and I wonder if you'd like to make some further comment
6 on this point, what are some factors that you think have had an impact on your ability to
7 raise capital?

8 **Ms Balle:** So as mentioned in our written submission there are difficulties obtaining capital to
9 support scaling. And there are several reasons for this, right. So, there are two that I
10 want to mention here.

11 And the first and foremost is the nature of the grocery sector in NZ, being a
12 duopoly environment. Investors are nervous about the tactics that the two players will
13 employ to block or restrict a new entrant, such as ourselves, and this has definitely been
14 our experience when speaking with more than a thousand NZ potential investors over the
15 past 3 months.

16 The second point I want to make is that the NZ capital market for start-ups, and
17 this is while it's getting better, NZ is not Silicon Valley. Internationally, where competition
18 is present, capital and investment flows as seen with online only operators around the
19 globe, for example, Gorillas in Europe recently raised 1 billion. Picnic in the Netherlands
20 raised €600m. In this year so far, we note that more than USD10b has been invested in
21 online-only grocery start-ups. But in NZ this is simply not the case.

22 To be able to scale Supie and provide access to consumers nationwide and on a
23 like for like, without bricks and mortar basis, we'll need access to more than \$115m in
24 capital. As much as we want Supie's ownership to remain in NZ, this is simply not possible
25 with the current conditions. However, we do believe there is a solution for this and we
26 can discuss this in one of the future sessions.

27 **Ms McWha:** I'd be very happy to talk about that now, Sarah, if that's possible, in terms of
28 recommendations, or ideas you might have around how we solve this.

29 **Ms Balle:** Yeah, so one of the opportunities that is present is, that we believe is a Kiwibank style
30 ownership model to enable Supie to be an effective competitor in NZ in operating in the
31 best interest of NZ, which is what Kiwibank prides itself on.

32 **Ms McWha:** Okay, thank you. Tex.

33 **Mr Edwards:** Thank you Commissioner. It's my experience in this matter, we're asking capital
34 providers to put capital in harm's way. That's what makes it different and difficult.
35 There's substantial scar tissue in NZ on challengers and NZ is quite different from other
36 environments because both our incumbent supermarkets have significant market power,
37 arguably it's a 50/50 duopoly, and the behaviours, the regulatory request here isn't
38 extreme, the behaviours of the incumbents have been off the record extreme! It's sort of
39 second page Financial Times narrative, you know, a 3-to-2-merger, a 20% raid on the third

1 operator's shares and this blocking of property covenants in NZ that's been banned in
2 Aussie.

3 Let's park that to one side. I applaud my industry colleague Sarah's comments on
4 the difficulty in getting capital. I think there's a swinging pendulum on whether we need
5 OIO approval, because essentially the NZ investors who would put capital in this industry,
6 are basically just wanting market power constrained and the issue is there's a double
7 jeopardy here because if there is a forced divestiture of incumbent supermarkets, the OIO
8 will push up the price available because there's always a discount if OIO isn't available or
9 not. So there's a two-tiered capital market in NZ for infrastructure as a consequence of
10 OIO. Maybe that's a submission point, I'll just park that to one side, I'll be delighted to
11 come back to that.

12 And I'll just share a real life experience in raising \$250m and putting it in at the ASB,
13 is my experience was, it took me something like 72-hours to raise \$250m after we had the
14 mobile market review published at 4 o'clock on October the 14th 2007, (thank you
15 Commissioner Webb, the Telecommunications Commissioner at the time) and that 42
16 page document when submitted to three capital providers, created a term-sheet. And it's
17 noteworthy, (of course we're in a different industry of course there are different issues
18 surrounding this framework) but that seed capital of \$250m which isn't fantasy land, it's
19 real money in the tin, came about because we had this 42 page document, written by the
20 Telecommunications Commissioner, covering off every barrier to entry, every regulatory
21 solution and he and the Commissioner at the time aligned NZ with OECD best practice.
22 Thank you.

23 **Ms McWha:** Okay, thanks Tex. Now just to briefly talk about the Overseas Investment Act. This
24 has been raised by some submitters in terms of hindering the speed with which overseas
25 firms can acquire sites. And I did just want to ask Woolworths briefly if they would like to
26 comment. Your submission Josh mentioned significant fees associated with overseas
27 persons receiving consent to acquire land. And I wondered, either now or later, if you
28 would be able to provide an indication of the total cost of making an application?

29 **Mr Gluckman:** Thank you Commissioner. James Radcliffe from Woolworths NZ will provide our
30 response to this question.

31 **Mr Radcliffe:** Thanks Commissioner. James Radcliffe from Woolworths NZ. Yes, we can provide
32 that information to you Commissioner, we'd probably prefer to do that later if we can, it
33 does vary and I think we noted in our submission that it does vary and we can certainly
34 provide those numbers to you. I mean, from our perspective, the Overseas Investment
35 Act is sort of law of the land, I guess, and we experience complying with it, we don't find
36 significant issues with it, we have a good relationship with the Overseas Investment
37 Commission. Of course it just applies to overseas companies and overseas investors and
38 we fall within that definition by virtue of the fact our parent company is Woolworths
39 Group.

40 That can make things a little bit slower, it just can take some time to get consent
41 and I guess, for some parties entering into a transaction, entering into it with an overseas

1 company, can be slightly disadvantageous because it needs to be subject to obviously the
2 consent of the OIC.

3 I think we can see benefits in simplifying it. We think that will make it even easier
4 for new entrants to enter the market, so we would support that. But I think, as I said, we
5 don't experience material issues in dealing with it and we'll certainly come back to you
6 with the detail you've asked for in the confidential session, or in writing if you'd prefer.

7 **Ms McWha:** Thank you. I think in your submission you suggested a class-based exemption from
8 the, I think, for supermarket operators. I just wondered if you had any comment on the
9 benefit of that exemption. I guess another option would be to have an exemption for
10 residential land acquired by supermarket operators only. So one of the things that, you
11 know, would be useful to sort of tease out a little bit is how the scope of any exemption
12 might be defined and I wondered whether you had any comment around that, James?

13 **Mr Radcliffe:** Thanks very much Commissioner. As I said, we don't have strong feelings about it, I
14 guess we, as I explained earlier, we are used to working under the current regime, we've
15 got good relationships with the OIC. Our sort of suggestions around class exemptions and
16 additional exemptions were really just in the spirit of responding to the call from the
17 Commission for us to think about any ways we could remove any difficulties or concerns
18 that a new entrant would find.

19 So we don't have strong views about it. It was just an idea in terms of removing,
20 you know, one potential barrier or constraint.

21 **Ms McWha:** Okay, thank you that's useful. I recall Eric Crampton, The NZ Initiative had some
22 comments around this point. I wondered if you would like to make any comment around
23 what options might be useful in terms of addressing the impact of the OI Act?

24 **Mr Crampton:** Thank you Commissioner. Yes, I worry that you might have had the wrong focus
25 in looking at the application fees for getting applications in front of the OIO. The real cost
26 that's going to be facing a new entrant would be in the capital that gets tied up for
27 months with uncertainty while you're waiting on an OIO approval process. The whole
28 session here has had something of a feel of an inquiry in the 1970s into the cost of cars in
29 NZ that went into access the Ford supply network and whether a Kiwi start-up might have
30 adequate capital that could have access to Ford parts suppliers. But didn't really look at
31 the consequences of the import licencing regime and bans on imports in materially
32 increasing the costs of cars in NZ. Getting rid of some of these barriers to entry and OIO
33 will be one of the material ones it seems important, I'd be happy to talk later also about
34 zoning on OIO.

35 If you guys have already decided that it's so much in the national interest to have a
36 new competitor that you would even go so far as thinking of something like Kiwi Grocer
37 which wouldn't work, for reasons that I can get into later, if it's that much of a national
38 interest, it seems ludicrous to have a national interest test for applications to buy land in
39 NZ to put up a supermarket. Just automatically approve them.

40 **Ms McWha:** Okay, thank you Eric, that's useful comment. The other question that I had around
41 overseas capital was, whether anyone had any comment about whether it's likely to be

1 less advantageous to the market overall than local capital. So thinking just about some of
2 these questions around how overseas supermarkets might source their products and that
3 kind of thing. Not wanting to put anyone on the spot too much, but I wonder if FGC had
4 any comment on this point? Katherine, are you with us this morning? Andy?

5 **Mr Matthews:** Sorry Commissioner, could you repeat the question please, sorry?

6 **Ms McWha:** Sure, I just wondered whether there was any comment on whether overseas capital
7 is likely to be less advantageous to the local market overall as compared to local capital?

8 **Mr Matthews:** I don't think we had a submission on this point.

9 **Ms McWha:** Okay, thank you. So let's move on to site availability. Submissions were largely
10 supportive of our options for addressing factors, potentially affecting site availability for
11 store development. So we'd like to focus the discussion this morning on the range of
12 options and associated costs and benefits for addressing covenants and other exclusivity
13 mechanisms. We'd also like to discuss the extent to which our existing options relating to
14 planning legislation would be sufficient to improve site availability.

15 Just very briefly and to ensure that we're all talking the same language, a
16 restrictive covenant is an encumbrance on the use of land which limits what it can be used
17 for. So in this case, excluding its use for grocery relating or a supermarket. An exclusivity
18 provision in a lease is an arrangement that gives someone the exclusive right to establish a
19 particular type of business in a mall or some other area.

20 And I'm going to use the word "covenants" to mean both of these things, but
21 please feel free to distinguish between them in your comments, if that's necessary.

22 So the first thing that I wanted to talk about was how we could address covenants.
23 One difference between the submissions of the majors was whether commitments could
24 be made on a voluntary basis or whether a law change was required.

25 Woolworths, so you guys submitted that you would support a law change. I just
26 wondered if you were able to speak to a little more detail about your suggested approach
27 and what you suggest would be the scope of affected covenants. James, is this something
28 that you would?

29 **Mr Radcliffe:** Thanks Commissioner, yes I can speak to that. We think this is an area where a
30 little bit of thought needs to be given and I think it's just in relation to some of the
31 complexities around the potential arrangements for site ownership. So, I think we spoke a
32 bit about it yesterday, some grocery retailers own their sites, others lease them, and some
33 sites might be owned by franchisees or owner/operators, or entities associated with
34 them. So as we sort of saw it and when we looked at this we felt there were a couple of
35 options.

36 The first one being a voluntary commitment from the grocery retailers not to
37 enforce restrictive covenants, sort of through to enforceable undertakings, which are
38 similar, I think, to the position in Australia, like, sort of right through to specific regulation
39 or legislation.

1 So as well as that, I think there needs to be some thought given and we'd be happy
2 to be involved in this, in sort of arrangements of the type you've discussed, that have a
3 similar effect to restrictive land covenants, that might be worded a bit differently. So for
4 example, a positive obligation imposed on someone to build or lease to a specific type of
5 retailer, so to a building products retailer or something of that nature might actually have
6 the same effect as a sort of prohibition on leasing to a supermarket. So we think once we
7 get into the detail, there'll be quite a few nuances of this, that we need to work through.

8 I think if the Commission's final recommendation is that steps do need to be taken
9 to remove these covenants, and we do support that, we ourselves haven't found a
10 material issue other than, I guess, some historic issues in relation to Wellington which we
11 can provide some information about.

12 We've certainly taken onboard the views of the Commission, and others actually,
13 that they do see an issue, so we support it. We do think that regulation or legislation is
14 the, probably the quickest and most efficient way to make sure that all of these types of
15 arrangements are sort of captured and can be unenforceable from the time the law is
16 passed.

17 So that's probably all on that point I have Commissioner, thank you.

18 **Ms McWha:** Thank you James, that's very useful. Perhaps if I could turn to Foodstuffs, Chris, I
19 wonder if you would comment. You indicated that you were willing to provide voluntary
20 commitments or binding undertakings not to enforce existing covenants or make further
21 use of them. And I just wondered if you could comment on why that's your preferred
22 approach and whether you have any comment on Woolworths' suggestions around
23 potentially making a law change?

24 **Mr Quin:** I'll pass to Mike Brooker for comment from a Foodstuffs NI point of view. We do have
25 a slightly different position between North and South Island, so we should be clear about
26 those, I'll pass to Mike.

27 **Mr Brooker:** Thank you Chris and thank you Associate Commissioner McWha and morena
28 everyone. Yes, we have come to our view, I guess, really from the position that we are in.
29 So we've got a portfolio where we mostly own our land. So it is relatively simple to give
30 away the benefit of those and we support that. We hear what the Commission has said
31 about land covenants and the like.

32 Slightly more complicated, I guess, in lease arrangements because they're bilateral
33 agreements and so there may be some challenges there, but we support the initiative.

34 If there was legislation or regulation, we'd just want to ensure that it goes through
35 due process and that we'd obviously seek to be involved in that process and we'd just like
36 to make sure that it doesn't have unintended consequences.

37 So yes, very committed to the position that we've outlined. We can do it relatively
38 easily in our case, but that's specific to us. Support the initiative and will be involved and
39 can ensure that the outcome is achieved, thank you.

1 **Ms McWha:** Thank you Mike. I wonder if I might ask you one other question, which is whether
2 covenants are currently a significant impediment to developing new stores for Foodstuffs
3 NI?

4 **Mr Brooker:** I don't believe they are. You know, we've got people in our property team out
5 there all of the time, searching for the right properties. This goes to, sort of, some of the
6 complexity of land opportunities, it takes us a long time and we do need to ensure that
7 the land is correctly zoned. Sometimes we might have to subdivide land, etc, etc. So
8 we're looking out quite a way ahead.

9 But no, we don't encounter a lot of land that we're prohibited from by way of land
10 covenants.

11 **Ms McWha:** Okay, thank you. So Foodstuffs SI, am I looking to Mark Sullivan perhaps?

12 **Mr Sullivan:** Thank you Commissioner. I think, just to pick up on Mike's point, Foodstuffs SI has
13 never been stopped by a covenant in developing supermarkets down in this island either.
14 Probably the point with leases, and it can be a difficult area, is that landlords use
15 covenants to attract a diverse range of tenants and therefore attract a wide range of
16 customers to their premises. And this in fact helps them maximise their rental returns.

17 Equally, and this is perhaps the point that Sarah from Supie picked up with regards
18 to start-ups, the situations where covenants can give a new entrant an opportunity to
19 become established and grow, and or in fact they may actually be the difference between
20 a landlord attracting a tenant or not. And the other thing too with, I guess, large rental
21 developments, often covenants are used to get an anchor tenant. It's the anchor tenant
22 that then brings in other tenants and therefore helps the landlord get a good return on
23 their investment.

24 So, I think we need to be very, very careful here because as has been said
25 previously by other people, there could be a lot of unintended consequences if we're not
26 careful.

27 **Ms McWha:** Okay, thank you. It's probably useful then to turn to Supie or one of the other
28 potential entrants to ask whether covenants are a significant impediment in terms of
29 developing stores and whether any of the approaches that we've been discussing would
30 be useful in terms of addressing that. I see Andy Matthews, though, has his hand up,
31 perhaps we'll go to him first.

32 **Mr Matthews:** Thank you. Look, just a couple of quick points. FGC have submitted on this point
33 and I think, you know, some sort of low-level notification in perhaps the ability to call in
34 and review for the Commission could be seen as helpful. But just thinking about it further,
35 you need to think about what difference that may make to incentives and whether it may
36 increase the risk of potential land banking too, which would, obviously, potentially create
37 greater barriers to entry and expansion.

38 And on that, just looking at the Foodstuffs NI approach to its ROACE calculation, it
39 made adjustments to reflect property ownership, including assets held for development,
40 both land and buildings, and I know this has been an issue that's been looked at, overseas

1 that issue of land banking, I can't recall where the Commission's draft report got to on
2 that. But I think that's just worth bearing in mind in terms of the whole picture of land,
3 we've focused very much on some promises and I'm not sure where those have landed.
4 There's obviously some issues to work through, but it does tie into ownership as well, I
5 would have thought.

6 **Ms McWha:** Thank you Andy. Eric let's move to you now.

7 **Mr Crampton:** Thank you Commissioner. I think it's worth thinking through these issues in kind
8 of the order in which they cause problems. Covenants really couldn't be a problem if
9 zoning were very liberal and it was impossible for that to then be an impediment. So if
10 everywhere in a city were allowed to be a supermarket and there were no zoning
11 encumbrance, it would be impossible for covenants to provide a substantial barrier to
12 entry, cause you just can't covenant all of the land in the city. It's only under conditions
13 where there's very restrictive zoning, where there are very few sites that might be
14 available to setup a supermarket, that covenants can have any effect at all.

15 I really enjoyed the discussion at chapter 6 in the Commerce Commission report,
16 you guys did a fabulous job through there but what I was really hoping to see was a
17 mapping of how many properties are even allowed to turn into a supermarket in major
18 centres in NZ? Right start with that map. Where could a new entrant go for thinking
19 about the kind of entry at scale. You've talked about the importance of being able to have
20 a network out of large footprint sites that are going to matter.

21 For thinking about an overseas entrant, first they've got the hurdle of the OIO,
22 whether they can come in at all. They have to accumulate a set of titles with the
23 appropriate zoning, then make sure that those titles aren't already restricted by
24 covenants. Now you guys can have a process for determining whether a specific covenant
25 is anticompetitive or not, but striking to the root of the problem, might go a step back and
26 liberalise zonings that more places could be supermarkets that there's more potential for
27 entry kind of anywhere.

28 Otherwise you've got the spot where a new entrant has to accumulate sufficient
29 titles that aren't encumbered by zoning, or by covenants, wait on OIO approval across the
30 set of properties which can introduce long and variable lags where capital is stranded and
31 you're bearing this cost of capital while you're waiting on a decision. Then you're waiting
32 on long and variable lag in consenting processes of whether any of the councils will even
33 let you run a supermarket in that place and we just saw a case in Ashburton last week
34 where a plan change had determined that, well basically it's an anticompetitive council
35 plan. They said we don't want to have more competition with downtown, we're going to
36 bar new entrants in these new retail developments that are coming in.

37 When you have those kinds of conditions that substantially block entry, everything
38 else we've been dealing with here feels like counting angels dancing on tin heads relative
39 to the substantial regulatory and legislative problems in actually getting new entry.

40 So yes, covenants could be a problem given the extent of zoning encumbrances, it
41 will be great for the Commerce Commission to really quantify those to see how big the

1 problem is, whether there are substantial number of sites that could possibly turn into
2 supermarkets, I suspect that they're not. I've seen some maps suggesting that it's
3 basically only places that already have supermarkets in Auckland that could be
4 supermarkets, and those are going to be tied up often in covenants and often for good
5 reasons, right. If an anchor tenant comes in and assist with the cost of developing a new
6 site, there has to be some exclusivity arrangement or you're not going to be able to track
7 that investment.

8 Those can be efficiency conducive, it's the zoning behind it that's causing these
9 problems and I'll shut up now, thank you.

10 **Ms McWha:** Thanks Eric, I think that's a really constructive contribution. And perhaps I could
11 just sort of jump ahead slightly. So one of the other things that we wanted to discuss was
12 planning legislation and whether, given the timeframes, required to amend planning law,
13 there were short-term interventions that could be made under existing RMA. And I'm just
14 wondering, Eric, whether given your comments, you think it might be useful to make a
15 recommendation, for example, to councils who are reviewing their district plans around
16 these points?

17 **Mr Crampton:** Sure. So I noted that in chapter 6 you recognised that there's a RMA reform
18 process that's underway and that you were wanting to step back a little bit from
19 recommendations around RMA reform. Really, this is where the Commerce Commission
20 should be coming in into the RMA reform process so that competition can introduced as a
21 beneficial effect in all of councils planning, rather than something that's, well ancillary or
22 that they don't even think about.

23 Current planning processes, as best as I can understand them, planners will look
24 out at, here's a neighbourhood, it's got this many people, for every X number of people
25 you're going to need a supermarket therefore we're going to allow this many
26 supermarkets. They're not thinking about competition and baking it into the process so
27 you wind up with planning rules that substantially constrain entry and prevent real and
28 effective competition and block entry.

29 So it will be wonderful if the Commerce Commission could have some input into
30 the RMA reform process, introducing competition as something that's critically important
31 in council plans. If we're getting regional planning processes that aren't even thinking
32 about this, we're going to continue having these same problems across all of the areas
33 that are affected by zoning.

34 Similarly, when councils put up plans that have anticompetitive effect, I would love
35 to see a role for the Commerce Commission in coming in here and saying, "You know, if
36 we saw this kind of activity just in the private sector to stop new entrants, we would be
37 thinking about, well maybe criminal cartel procedures around this, you guys are
38 implementing it through zoning restrictions, maybe have another think about this". It
39 would be wonderful to see a more formalised role for the Commerce Commission in
40 looking over council plans to make sure that they are not, perhaps inadvertently,
41 stymieing effective competition.

1 **Ms McWha:** Thanks Eric.

2 **Dr Small:** Thanks for that Eric. So do I take it you're in behind paragraph 9.81 of our draft
3 report, it will be good to get any comments on that, I don't expect you to do that now, but
4 maybe in a submission would be helpful, that's where we talk about exactly the kind of
5 input into the planning law reform that you've been talking about there.

6 **Mr Crampton:** I don't remember paragraphs by number I'm sorry but we do support the
7 Commerce Commission coming in on these kinds of roles.

8 **Ms McWha:** Great, thank you. I'm conscious that we don't have a lot of time left and we've got
9 some hands up, so let's just go to, I'll turn to Tex then James and Mike, so Tex.

10 **Mr Edwards:** Thank you Commissioner. I'd ask the Commission to look at the intended
11 consequences of these covenants. The horse has bolted. We've had entrenched
12 behaviours for 15-years and I'd ask the Countdown executives to consider that these
13 behaviours have been banned by the ACCC in Australia for 15-years and it really breaches
14 the social responsibility covenants and the GRI report inside the Countdown ecosystem.

15 So the issue is, please look at the intended consequences because it's raised the
16 cost of capital for a challenger and you've had these entrenched behaviours which really
17 need to be discussed in the regulatory prescription.

18 Closing off on my previous speaker's comments, there's a wonderful submission
19 point where we actually listened to a Countdown employee talking about when the
20 Countdown at Highland Park in an Auckland suburb called Howick, a Countdown is right
21 next to another Countdown, it used to be a Countdown next to a Foodtown. Her exact
22 comments were, "We loved having the competition next to us, it used to keep us on our
23 toes". Thank you.

24 **Ms McWha:** Thanks Tex. James, perhaps I could come to you now.

25 **Mr Radcliffe:** Thanks very much Commissioner, I'll keep it really brief and it's sort of, I guess from
26 a personal perspective, it's great to be involved in the process and it's sort of fascinating
27 to hear the views of everyone else cause you sort of get a bit blinkered, I guess, and as we
28 said, covenants for us hasn't been a major issue. But we've certainly heard for others that
29 we have and we've given the sort of commitment. And I guess we looked at the
30 experience in Australia and that was mentioned by Tex, thank you very much, and in
31 relation to the sort of commitments given by the grocery retailers, the ACCC did say that
32 releasing those actually increased the number of shopping centres with more than one
33 supermarket. And I think in relation to the experience we did; they did see Aldi grow from
34 170 stores at the time of the undertaking to 590 this year. So clearly, it can have quite a
35 material effect and I guess in the spirit of cooperation, that's why we support and have
36 given our commitment. Thanks Commissioner.

37 **Ms McWha:** Thanks James. Mike.

1 **Mr Brooker:** Thank you Commissioner and I'll be brief. Look, it's really interesting to hear this,
2 it's so funny to hear the talk about RMA when we're the poster child for the longest
3 running RMA case, ever, and I believe Commissioner Small is very familiar with that.

4 I'll just make a few comments. The current land covenants, if the purpose or effect
5 of those was anticompetitive then they'd be illegal today. We've heard a bit about
6 blocking. I think the Commissioners will be extremely well aware of the provisions in the
7 current Commerce Act about unlawful blocking, so those are there.

8 In terms of how we might respond to entrance. I mean I think there's been some
9 suggestion the response might be untoward. I would phrase it as the response will be
10 competitive and that's of course what I think the Commission is looking for. So you know,
11 a competitive response is called for and that's what we're up for.

12 Land banking has been mentioned. Now this is a term that I think is incredibly
13 pejorative. We don't land bank, if that's a term that means that we hold assets for the
14 sake of holding out others, we strategically buy land well ahead for the reasons that I've
15 described, and we need to do that to ensure that we can provide supermarkets for our
16 customers in the future cause it takes a long time.

17 Disruption is here and it continues to come. It will come from all sorts of manners
18 and mechanisms.

19 And just on barriers to entry, so the point about barriers is deduced from the fact
20 that the Commission has found extremely high profitability in our industry. Now, as you
21 know, we dispute that. So entry's all about opportunity and if the opportunity is
22 overstated, then you might come to the view that there's high barriers. But we obviously
23 contend that that's not the case.

24 And then just a final point, and we talk a lot about a duopoly and we do accept
25 that there are only two players in the main order supermarket market. But the point
26 we're making and I think it is very different to some of the other industries that we've
27 looked at and commented on here, is that while there may only be two players in that
28 part of the market, there's still choice. And in a duopoly, say airline, say telco, etc, if
29 there's not another player, there is no other choice.

30 So that's what I'd like to say, thank you.

31 **Ms McWha:** Thanks Mike. Now, we really have come to the end of our time this morning and I
32 would like to thank everyone for their constructive contributions. I'm aware that we may
33 not have got across all of the comments that everyone would like to make.

34 One other issue that I just did want to raise very briefly, because it has come up in
35 a number of submissions, is, as a competitive disadvantage, is the inability of some stores
36 to stock alcohol. As you'll appreciate, alcohol sales regulation has important social policy
37 objectives and these are outside the Commission's remit, so it's not something that we
38 were proposing to discuss today. We have heard the submission about the impact of
39 these regulations on competition.

1 One specific point that we would be interested in additional information on, via
2 our submissions process, if anyone has this information, is in relation to any observed
3 differences in the ability of stores that are not able to sell alcohol to compete in areas
4 where local licencing laws mean that supermarkets generally are not able to sell wine and
5 beer. So if anybody's able to inform that specific point, then it would be very useful if you
6 could send us some evidence on that.

7 Otherwise, as I say, thank you very much for your contributions this morning.
8 After the morning break, we will come back to talk about access to wholesale supply. If
9 you have further submissions on any of the issues that we've discussed this morning, or
10 any other conditions of entry or expansion that you think are relevant to competition,
11 then please do send the additional material through to us by the 23rd of November to our
12 email address, marketstudies@comcom.govt.nz. Thank you and we'll see you at 11.15.

13
14 **Dr Small:** Good morning everyone, welcome back to session 8 of the conference and we're going
15 to be talking about further conversation about improving conditions for entry and
16 expansion, focusing on wholesale supply of groceries.

17 So, as you all know, the Commission's draft report found, and this might not seem
18 an obvious point, that a grocery retailer cannot provide a widespread full range
19 competitively priced offering without first obtaining groceries at competitive prices, either
20 from a range of suppliers or from a grocery wholesaler.

21 Wholesale groceries could, in the future, be obtained in a number of ways, through
22 voluntary commercial arrangements, is one option. Another option is an enforceable
23 access undertaking, which would be given by major grocery retailers. And a third option is
24 a regulatory access regime.

25 Submissions were somewhat divided in their views on these issues and so it will be
26 important to test some of these issues and areas of difference today.

27 So the plan for this session is to start really by looking at the desirability or
28 necessity of improving wholesale access as a way of stimulating retail competition. And
29 then we'll look at the feasibility of doing that. And finally about the potential options for
30 arranging and governing improved wholesale access, should that be considered necessary
31 or desirable.

32 There's quite a bit of material to get through, but I think we've got the time and
33 I'm sure we've got the people around to do this.

34 So, starting with the first question of, is access to wholesale products or improved
35 access to wholesale products necessary or desirable for entry or expansion?

36 As you know, we said that a lack of access to a wide range of wholesale groceries
37 at competitive prices is a key factor preventing entry and expansion of grocery retailers
38 and so we did look quite closely how to improve that.

1 So I want to test two propositions about how efficient wholesale access
2 arrangements could promote competition. One is that it could do that by reducing a
3 barrier to expansion for existing grocery retailers that are already there but could expand.
4 What we called 'other grocery retailers'. And the second is by reducing a barrier to entry
5 by one or more large, new, at scale, grocery retailers.

6 In submissions, Foodstuffs has submitted already on both of these points, arguing
7 that wholesale access would not promote competition from other retailers and the reason
8 given was that 68% of the shelf price is the product cost, so other retailers would only be
9 competing over the remaining 32% of costs. And Foodstuffs also said that better
10 wholesale access wouldn't promote competition from larger scale grocery retailers
11 because they would be vertically integrated.

12 So, I'd like to hear, first of all, if we could from the two smaller retailers that we've
13 got here with us today, that would be Night 'n Day and Supie, on the first of these points
14 and we've already heard some comments on this. But I really want to probe on the
15 necessity, how crucial is this for you to provide better competition with the major retailers
16 and then I'll come to Northelia which I think is Allan Botica to talk about the other end of
17 the entry and expansion spectrum.

18 So, is Matthew Lane available to kick us off on this point?

19 **Mr Lane:** Yes, certainly I'm more than happy to cover the point there. And look, if I was to sum-
20 up our whole barrier to entry in this grocery area it would centre around the ability to
21 obtain wholesale supply. So I'm really glad we're zeroing in down on this and I think
22 there's two aspects to wholesale supply.

23 One is access and you've said that through voluntary enforceable or regulatory,
24 but voluntary access is available at the moment and it sort of hasn't really worked as
25 planned, I would say, in terms of creating a really cohesive relationship as you'd expect
26 with commercial terms associated around it.

27 Enforceable, I guess wholesale supply still begs the same issue is that it doesn't
28 actually detract any market share from Foodstuffs or from Progressive. It still gives them,
29 it still enhances their buying power with suppliers, it doesn't allow the suppliers to branch
30 off and be able to form new relationships and work largely directly with the customer as
31 well.

32 So, look, for us, we do see wholesale access as an issue, it's easy for Foodstuffs to
33 say it isn't an issue when they have one of two avenues available to them to obtain it.
34 They control the wholesale as does Woolworths. And there's no plan C. There's a plan A,
35 there's a plan B, and a plan C so far removed is actually not really a feasible option.

36 They have also got voluntary supply through Trents and Gilmour and we've seen
37 there through some of the data that I've submitted in my submission it's 43% more
38 expensive.

39 So without being able to obtain products at a cost-effective price, it's impossible to
40 build market share. We give a lot of commercial sensitivity data to those major retailers

1 through purchasing through them. Which same thing is, if we're actually going to talk
2 about breaking down a duopoly and we're talking about a large increase in terms of the
3 market share, by simply redirecting the funds to them through a different mechanism, it's
4 actually never going to achieve that.

5 I think voluntary could work in terms of supply. If we had increased competition in
6 the market with three or four or five players in there, all of a sudden the volume that we
7 do currently have can be leveraged across those wholesalers and actually create a
8 demand for that business.

9 There's no real demand for our business at the moment, there's no real willingness
10 to work with us. As a result of that, we can't obtain competitive prices, we can't pass on
11 competitive prices to the customer, so if customers want to obtain competitive prices,
12 they're basically in the hands of Progressives or Foodstuffs wholesale network.

13 **Dr Small:** Thank you Matthew, that's an interesting set of comments there, there was a few
14 things that we will pick up a little bit later on, but I note your comment that things would
15 be different for you if there were three to five wholesalers in the market already rather
16 than, what you see is two options. And I noted also the point about commercial sensitivity
17 of data, so we will come to those a little later on. I wonder whether Sarah Balle would like
18 to make any comment on this from Supie's point of view.

19 **Ms Balle:** Yeah, thank you, I'll keep it brief. I would just like to reiterate Matthew's comments,
20 access to wholesale supply is very important. It's absolutely necessary, the options
21 available at the moment are just not viable. And as I mentioned at the start of today, it's
22 not just from a cost perspective but the range of product offerings and the sufficient and
23 consistent supply.

24 And just touching on the point from Matthew in terms of the data that the
25 incumbents would have if we were to get wholesale supply via their networks, so there's a
26 range of issues within that and yeah, being able to enter the market, that would have
27 made it a lot easier for Supie. Obviously we've now created our own wholesale supply, it's
28 not perfect at the moment cause we did create it ourselves over an 18-month period
29 which was a huge investment for us, but was necessary because there were no other
30 viable options in NZ.

31 **Dr Small:** Thanks for that. So could I just probe a little bit on that. So you've already got some
32 kind of supply network with direct relationship with suppliers, so from this point of view,
33 you're saying that from this point on it would still be, could you talk about the marginal,
34 how much extra benefit would you get and what would that do for your business and your
35 ability to compete now from the point where you've actually got some kind of relationship
36 with suppliers, what difference would it make to have wholesale supply from here?

37 **Ms Balle:** Yeah, so from here, now that we largely have a similar set of suppliers, at least over the
38 next 6-months we'll have a similar number of SKUs from a main shop perspective. From
39 here, its more around pricing now that we do have access to product range and secure
40 sufficient supply. But yeah, pricing is definitely limited because we don't have the scale
41 that the incumbents have, right, so that's an issue.

1 **Dr Small:** Thank you, that make sense.

2 **Ms McWha:** John can I just ask Sarah whether you've considered joining with another or a
3 number of other retailers to obtain a greater scale for this wholesale or providing a
4 wholesale service to other retailers?

5 **Ms Balle:** Great question, for us at Supie, we didn't realise that it was an industry wide issue
6 accessing wholesale supply across the other retailers until the conference. So it's
7 definitely an opportunity, however we have to note that the market share of all of the
8 fringe players is still not that great. So yeah, we still have that scale issue largely, as well
9 as infrastructure. So from Supie's perspective, give that we're online only, we have our
10 order fulfilment centre as well as our DC combined, so that's an advantage for us because
11 we're not having to send out to many bricks and mortar stores across a network or across
12 the nation, we're all centralised. So from an infrastructure perspective, we're okay, but I
13 can see how that is an issue for bricks and mortar entrants or creating that competition
14 for them.

15 **Ms McWha:** Thanks Sarah.

16 **Dr Small:** That's great, thank you. Yeah, helpful comments, perhaps we turn to the other end of
17 the scale spectrum now and I wonder if I could call on Allan Botica, I think you've got some
18 views on this and might be an opportunity for you to give us your broader views if you
19 could do that too, thank you.

20 **Mr Botica:** Thank you very much. Access is obviously important but the conditions on access are
21 as important as the fact of access itself. We've heard mention of the long timeframes that
22 are involved in property, equally long in development.

23 Now Northelia offered in its submission to deliver a new like for like supermarket
24 chain. For this to occur, the following conditions, minimum conditions would need to be
25 met while Northelia's own infrastructure is being built. The first 36-months of
26 comprehensive access to wholesale on a non-discriminatory basis, this would include full
27 equivalence of capability with the incumbents, full accounting separation, and non-
28 discrimination on pricing terms and service levels.

29 Secondly, the appointment of a Supermarkets Commissioner for a term of 5-years
30 with the power to make immediate and binding decisions.

31 Thirdly, legislation to prevent pocket pricing.

32 And fourthly, a declaration of SMP (significant market power) by the Commission
33 to the incumbents.

34 Now, those represents Northelia's position on what it would take to get a new
35 large scale, like for like competitor. Thank you.

36 **Dr Small:** Thanks for that Allan. So a useful list and on the narrow question of wholesale access
37 you've emphasised the conditions of access and you've also emphasised that it would be,

1 from your purposes, that a time limited access would be enough. I will take one
2 comment from Katherine Rich and then we'll move onto the next topic, thanks Katherine.

3 **Ms Rich:** Thank you. Yes, the point that getting supply and access supply is being critical is the
4 main point here. And often within the supplier community, it is extremely difficult to
5 supply new entrants, particularly for the small to medium size companies. And the reason
6 for that is risk to their business and fear of repercussions because there've been cases
7 where suppliers have supplied new entrants and the most recent case study would be The
8 Honest Grocer, where the incumbents will apply pressure, either directly to suppliers, or
9 indirectly as a result of the environment. Suppliers know for an easy life, sometimes it is
10 easier not to supply even though they want to be helpful and support new entrants. It's
11 just too much of a risk to their business. Thank you.

12 **Dr Small:** Thanks for that. So look, I think that wasn't directly on retail competition but it's a fair
13 point any way. Can I go to the next question which is, is wholesale supply feasible? So
14 we've talked about would it be necessary and helpful, is it feasible and then we can talk
15 about the rest of the topic later.

16 So, Woolworths NZ in its submission said that wholesale supply is feasible,
17 although it's complex. It's obviously complex, we'd all agree with that. And helpfully
18 outlined a set of issues that would need to be worked through carefully including supplier
19 rebates, that's back to the supplier side that Katherine was just talking about, supply chain
20 capacity, questions about service levels, obviously, and fulfilment times, and wholesale
21 capability.

22 Foodstuffs in its submission didn't actually really directly address feasibility, but did
23 make other comments on the complexities which we agree with. And Foodstuffs pointed
24 particularly to questions about the range, the number of products involved, the lack of an
25 existing market and the uncertainty of demand.

26 So if I could just start with Foodstuffs on some of those questions just to explore
27 those, these are about the feasibility and it's also, I guess, frankly about the mechanics of
28 wholesale supply.

29 So I see Chris Quin you've got your hand up so perhaps you could deal with these
30 for me. I guess the first questions is, I mean wholesale access does occur in other places
31 right, we've got the example of Metcash in Australia. And so does that sort of, that
32 suggests a degree of feasibility, would you agree with that and do you want to make any
33 other comments on the complexities and the issues?

34 **Mr Quin:** Thank you Commissioner. So look I think the first statement I'll make is we have an
35 open mind to wholesale supply on commercial terms but there are a set of issues which
36 have been actually pretty well covered in this morning's conversation. I think Allan
37 Botica's review of all the things that might need to exist in a regulated environment are
38 part of what you would need to consider.

39 I think the first thing, this morning's conversation examined almost is the issue
40 access to product price and product or is it supply chain? And I think probably we would

1 say it seems to be a lot more about product and product price than supply chain based on
2 the availability of partners.

3 The second thing is, you know, we're not currently a wholesaler and I'll deal with
4 Gilmours very briefly, separately even though I think there is an assumption from some
5 views that we are, we're not setup as a third-party wholesaler. Metcash probably
6 deserves more conversation because it is a supply chain and franchisor to a set of brands,
7 not a market wide wholesaler as such. The second thing and it's been clear through the
8 conversation, it's unclear who would use the wholesale service for what period for what
9 range and what demand. And what period of time they would want to use it for. So
10 establishing the business case and the returns required and those things would need some
11 work and is one of the complexities.

12 From a Foodstuffs point of view we would need to create new business capability,
13 the ringfencing, the confidentiality, the customer service, the account engagement. A
14 number of people on this conversation are familiar with the journey telco went through
15 for that, which is a very different market with a single copper network asset, very unlike
16 this market. And this is way more complex in terms of supply. So we're not ready to go
17 with something to turn on. This would need a lot of work to build and to put in place
18 against an unclear demand issue as such, given that larger retailers that are arriving are
19 establishing without wholesale because they can deal direct.

20 I think the other really important piece is to understand how much of the scale
21 value that large players get is due to volume, and how much of the price difference is due
22 to trade and marketing terms from suppliers because they are different and can't be sold
23 just with volume as such. So I worry that there's a slight assumption that says volume
24 automatically changes all of the terms and it doesn't. There is quite a lot of what makes
25 up the final cost of a product on shelf that sits inside supply decisions around where to
26 apply trade and marketing support.

27 And if I just go briefly to Gilmours while we're talking about that. Gilmours do
28 benefit from our volume and we support that brand with that but do not benefit from a
29 lot of the trade and marketing spend. They also need to effectively add their service in
30 the way those stores are run or delivery or account management or credit sales and all
31 those sort of things. And that is a big part of the reason why the difference between a
32 high-volume retail product with none of those services and none of the trade spend is a
33 different price to a Gilmours product for the same thing.

34 So I think they're all issues that need to be considered as you go, is there a solution
35 that will actually deliver the product range and price story.

36 And the last quick point I'd make is range has quite an impact on supply chain
37 because carrying more volume of a smaller set of products is quite a different proposition
38 and operational constraint than carrying a very wide range of a wide range of [inaudible],
39 etc.

40 So there's some of the things we think about as we think about the feasibility and
41 how you would do it and where we sit now, thank you.

1 **Dr Small:** Thank you very much. That's a really helpful contribution, I greatly appreciate it. I
2 think the question about who would use it and for what period, is one of the reasons that
3 we're kind of interested in and one of the advantages of an arrangement that relied on
4 Foodstuffs and Woolworths I think, so that's a useful point to make.

5 Can I just check that when you talk about the price gap, and saying it's maybe not
6 just volume related but is also related to trade terms, which I think you called trade and
7 marketing support, would it be fair for me to, in my mind, to link that to the supplier
8 rebates that Woolworths mentioned explicitly, is that correct?

9 **Mr Quin:** I believe so, but Woolworths should comment given its their term. And I think this is a
10 conversation we could pick up in more detail in a confidential session, but I think the point
11 is quite important to make.

12 **Dr Small:** Yeah, I do too. And I also thank you for this distinction that you've made between
13 product and price on the one hand, and access to supply chain as a possible second hand.
14 And so I think that's something for people who may be wanting to get access to think
15 about as we move through this conversation, is it both of those things or is it mainly
16 product and price?

17 So thank you very much Chris, that's very helpful. Tim Donaldson from Foodstuffs
18 SI, you've got your hand up there, would you like to add to that?

19 **Mr Donaldson:** Yes, thank you Commissioner. Look, I won't repeat the points already made but
20 just to say that wholesale supply to other retailers by Foodstuffs SI is theoretically feasible.
21 But of course we'd need to address all of the considerations that were raised in the
22 Commission's draft report and many more which have just been highlighted.

23 But I think it's really important to state cause I don't think it's well understood,
24 that we do not have separate wholesale and retail functions in our business. We're a fully
25 integrated supermarket business that purchases products from suppliers and sells to
26 customers. So it's not a simple process of drawing a line between those two concepts. So
27 that means we'd need to build the technical and infrastructure capability required to
28 wholesale to third-party retailers.

29 So we believe there'd be a lot of considerations that have to be addressed. But it
30 would be theoretically feasible for us to wholesale, but it would need to be done on, in
31 our view, normal commercial terms, and that's something that we certainly wanted to
32 emphasise. Thank you.

33 **Dr Small:** Thanks, that's a point that we'll have to come to obviously and we've talked a little bit
34 in the draft report and its come up previously about non-discriminatory terms, so we'll
35 come to that in just a tick. But can I just put it to you though that while we've got you
36 there, is that, from the outside, you know, what's known is that Foodstuffs started off as a
37 buying coop, I know you've evolved a lot from there. And all your stores are
38 owner/operated and that's a big part of the attraction for many people. So it does look,
39 you know, at that high level like a system where there's a kind of a wholesale
40 arrangement for goods that get sent to all these individual stores.

1 So it bears a lot of resemblance to a wholesaling operation so it's a question of the
2 functions is it that's captured within the wholesale, what is in the wholesale function, is
3 that the issue that we would need to grapple with and how to draw a line around that?

4 **Mr Donaldson:** Look, I think they're good questions Commissioner and they're probably for a
5 confidential session but at a high level, it's very much around the fact that, you know, the
6 members operate their own store, they also own a part of the company that provides
7 services around marketing, support, procurement and distribution. But I think, you know,
8 we provide within the cooperative distribution and supply chain, rather than wholesaling
9 services to our members. And I think it's also really important to understand because
10 we're having this conversation around access to products that 49% of the products that
11 our members retail, come direct from suppliers.

12 **Dr Small:** Okay, thanks. Chris Quin wants to chip in here as well and since we're engaging with
13 Foodstuffs on this point, this is a good time.

14 **Mr Quin:** Thank you Commissioner and I'd put my hand up before Tim started, so Tim covered
15 well. So I guess the key point we'd make is our owners own a single store and the
16 business and perform a number of the functions to deliver a retail offer to the customer.
17 And they are a part-owner in a shared services for marketing, for HR, for finance, for
18 supply chain, for buying and all of those things. So they are not, this is not a wholesale to
19 a store business model. It is a single business model with the parts centralised or localised
20 depending on what makes the most sense from a customer offer point of view. So it does
21 not resemble, there is not a breakpoint at which you could simply say that's the wholesale
22 point, there isn't one. And I think the analogy has been used in previous conversations of
23 it's a single functioning body, rather than series of parts in different buckets. So just to
24 finish that off, thank you.

25 **Dr Small:** Thanks, that's a good point about part ownership with shared services, I appreciate
26 that. So there's a few other people with their hands up that have been waiting for a while
27 so I'll just perhaps get perhaps Ernie Newman could give us his thoughts on this particular
28 point.

29 **Mr Newman:** Thank you Commissioner John and kia ora everyone. I'm Ernie Newman, I'm a
30 semi-retired consultant from the Waikato and I've spent a large part of my career
31 managing different industry organisations and interestingly they included 12-years
32 running TUANZ the Telecommunications Users Association while the separation of
33 Telecom was going on. And well before that, I was executive director of the Grocery
34 Manufacturers Association in the early 1980s and that was the organisation that went on
35 to become today's FGC. So I'm a predecessor to the job that Katherine Rich now does.

36 So the session's about entry or expansion but of course there is a third option and
37 that's separation. And from that perspective I think it's worth just looking back over a wee
38 bit of history to see how the industry is now compared to what it was 40-years ago.

39 So, in those times I recall far more retailers than we have now. I remember in
40 Wellington alone where I lived there were at least 10 different competing retailers. And
41 more importantly there was much greater separation among the three tiers of the

1 industry, manufacturing, wholesaling and retailing. And that was underlined by the fact
2 there were there strong industry organisations. There was NARGON, (the National
3 Association of Retail Grocers and Supermarkets) and that was chaired by a New World
4 owner from Upper Hutt.

5 There was the NZ Wholesale Grocery Federation, the chairing of which rotated, I
6 think, between Woolworths and Foodstuffs. And I'd have to say that some of the previous
7 people in that role would turn in their grave to hear Chris Quin say that Foodstuffs is not a
8 wholesaler because they categorically did position themselves as such in those days.

9 And then the third group was the GMA, now the Food and Grocery Council.

10 So at industry conferences and the likes, there was always three strong
11 perspectives with wholesale and retailing having quite different views. And the wholesale
12 arm was always trying to gain the ascendancy but retailers were a very independent
13 bunch and had views of their own.

14 So, my key point on that is that the power in those days was much more evenly
15 balanced. The manufacturers were fortunate in those days that we had import licencing
16 and tariffs so it was difficult to import products in competition. Wholesalers appeared to
17 be willing to supply retailers who were not necessarily tied to them through the
18 ownership of banner groups and I think in those days, Night 'n Day and Supie would have
19 found themselves very much welcomed into the industry and probably having competing
20 wholesalers vying for their trade.

21 And the power of manufacturers was much greater and we've heard a lot of
22 stories about the, I guess my word, 'intimidation' that suppliers feel from the duopolists.
23 But in those days I remember that some of the retailers were slow payers, notoriously,
24 and the manufacturers could quite happily cut off supply as an incentive to them to pay
25 their bills. So the balance of power –

26 **Ms McWha:** Excuse me, sorry.

27 **Dr Small:** Ernie, we really are talking here about the feasibility of wholesale access, so these
28 points are useful background, but have you got something specific on the feasibility of
29 wholesale access?

30 **Mr Newman:** Absolutely Commissioner. So my point is that wholesale access has been done
31 before in an independent way. We look back on history 40-years, it worked extremely
32 well in this industry. It has worked very well in other industries also.

33 **Dr Small:** Thank you for that. I think we're aware that it has worked, both of the major grocery
34 retailers said its feasible. There's a lot of complexities to work through and what we're
35 trying to do now is just spend a little bit more time on a couple of those particular
36 complexities and then I want to move on to talking about the framework in which this
37 might happen. And I'm going to ask the people that have their hands up, which is
38 Matthew Lane and Hans Maurer, about these two points which seem to be important.

1 One is about own brand products and would you, or more generally the range of
2 products to which wholesale access would be required or sought?

3 And the second one is about the terms and the concept of non-discriminatory
4 terms and whether or not that's feasible and a reasonable approach?

5 So could I start with Matthew Lane on that please.

6 **Mr Lane:** Yes, thank you. Without regurgitating what was touched on I just wanted to reiterate
7 the point that Foodstuffs were a wholesale mechanism and has more than capability to be
8 able to provide it in the past, so I don't quite know where this disconnect has happened.
9 That all of a sudden there's a whole heap of complexities underpinning it. I think it's being
10 overshadowed a bit; they can do wholesale supply down in Haast why they can't make
11 wholesale supply to us. And I also want to make sure to doublecheck in terms of what
12 wholesale supply is defined as because I note that there's a lot of chat about the Chemist
13 Warehouse, direct to store, which I suspect is Coke Cola and Frucor and the like. But the
14 overall point of this study is to reduce the household shop to consumers. I think the
15 wholesale supply needs to focus on that core dry grocery product that is being restricted
16 to what retailers can get access to. Everything stems from there, the main shop stems
17 from being able to get some sugar, some flour, some baby food, some pet food at
18 competitive prices.

19 So I think while wholesale is an issue, it's wholesale around the control they have
20 and have no willingness to overall supply and have a commercial benefit by blocking every
21 competitor coming into the market.

22 Around terms, look we've got terms with 150 suppliers and they're all commercial
23 terms. And they all work very productively and I think the key difference with those
24 suppliers that we work with, if there's not such a direct correlation between the suppliers
25 and actually being retailers, Coke Cola, Frucor, Tegal and the like, they are all traditional
26 wholesalers. We use wholesalers like BidFood, the same thing there, wholesaler, they
27 don't retail to the general consumer. And as a result there's a lot more ways to work but
28 also commercial terms that you can obtain and your actual bargaining power, when you're
29 trying to obtain them is significantly different.

30 The position we're in with the current wholesale and the terms that we're faced
31 with, is ultimately we take what we're given. I think that's a very dangerous position for
32 anybody trying to grow market share that you don't have an ability to be able to negotiate
33 with comfort there's a plan B in place, to the point if you – same as what we've heard
34 from suppliers, if you negotiate too harshly you can actually lose the supply or the
35 opportunity altogether.

36 So, terms would need a lot of discussion. I don't know how that can be enforced, I
37 don't think it's a question for hearing now because it's so wide ranging and the
38 implications of it.

39 **Dr Small:** Thanks for that. And I think I remember I was going to press you on own brand but I
40 recall the other day that you mentioned that one of the effects of own brand is to sort of

1 increase the price disadvantage which you were at, so, well perhaps I will press you on
2 that, does that mean you would want access to own brand?

3 **Mr Lane:** We would certainly want access and I also think there's quite a difference to what
4 Woolworths have done verse Foodstuffs have done with their own brand and Sarah
5 touched on it, it really resonated with me, where Woolworths own brand is recognisable
6 as Woolworths own brand, whereas Foodstuffs own brand is Pams, is totally segregated
7 away from any actual knowledge that it is exclusively available to Foodstuffs. And I think
8 that there does deter the customer in terms of, why don't we stock Pams and the like as
9 well.

10 Certainly access to own brand would be advantageous if we could have that same
11 thing as part of the wholesale network, but same thing, by buying it and selling it, we're
12 just increasing the buying power of the major grocery retailers to the overall supply and
13 we've heard about the implications of own brands on those primary suppliers.

14 **Dr Small:** Thank you. Okay, I'm going to go to Hans and then I'll come to Jo Allan from
15 Woolworths.

16 **Mr Maurer:** Thank you Commissioner. From a fresh produce point of view and that is the
17 interest of my organisation here, is that we are in this instance different to the rest of the
18 grocery range because we have a working and viable wholesale environment that is
19 capable of coping with competition. And the key here, from our point of view is this, is
20 that all the changes that you've talked about for the last 4-days have been experienced by
21 the produce value train as well. Whether they're growers, wholesalers, or retailers. And
22 yet, our wholesale system is also still in place despite the fact that the large supermarkets
23 increasingly start buying directly from growers.

24 And the point I'm trying to make here is this, wholesale within the perishable area
25 reacts. It reacts to regulation and deregulation and it reacts to strategic retail changes. So
26 in science terms, think of wholesale in produce as an amoeba, it changes shape depending
27 on the strategic landscape it operates in.

28 On that basis, I have some sympathy with Chris Quin's view, that how do you
29 actually maintain a degree of flexibility and find the money to invest into a wholesale
30 operation if there are limited certainties available in terms of risk management.

31 **Dr Small:** That's a helpful point actually. If you don't mind I'll move now to Jo Allan, I apologise
32 Jo Allan for calling you a Woolworths person first, so would you give us your contribution
33 on this please.

34 **Ms Allan:** Thanks Commissioner, no, I haven't transferred to Woolworths overnight.

35 **Dr Small:** Sorry about that.

36 **Ms Allan:** Sorry Josh. Look I just wanted to respond to Matthew's comment just around the
37 complexity and Chris did touch on some of these points earlier, but I think it is just worth
38 covering off a few more of the complexities. Although we certainly do think that it's
39 feasible to operate a wholesale function within our organisation or to provide that

1 capability, the key point is we have already pointed out is that to access competitive
2 pricing, I think you certainly need to distinguish between the promotional price and the,
3 what we'd call, the purchase price, because the two are very different.

4 Coming back to terms of trade. Absolutely, we'd need to define appropriate
5 wholesale terms and conditions, they need to be agreed, they need to cover things like
6 ranging, minimum order quantities, duration, guarantees, supply pricing, all of this would
7 need to feed into what infrastructure we need to build as well and I think the point's been
8 made that we currently have 80,000 products or SKUs. But we don't have them all in our
9 DC. If we were to bring them into our DC, we would need to essentially build extra
10 capacity.

11 Now, this then becomes a supplier question, probably first and foremost because a
12 lot of our suppliers do deliver directly to our stores.

13 Now, suppliers and the comment was made yesterday by Hexis Quadrant that we
14 bring suppliers into our DC and we transfer the cost to the suppliers. That's factually
15 incorrect and I do want to refute that statement. Basically, suppliers come into our DC
16 by choice and they make that choice based off what's the best cost to serve for them. So
17 what's the best commercial arrangement for them? Is it cheaper for them to deliver
18 directly to a central warehouse or is it cheaper for them to deliver directly to a store? So
19 that becomes a supplier challenge. And I think that that just needs to be, that point needs
20 to be understood.

21 Coming back to margin as well, and all of this would obviously need to be
22 considered at an arm's length margin and I think just finally, the only point I would also
23 just like to make is that Gilmours currently does offer wholesale pricing to its customers.
24 It offers wholesale pricing at a cost to serve and it costs more to deliver to a number of
25 smaller stores with smaller order sizes, etc. So that also just needs to be understood in
26 the value chain. Thanks.

27 **Dr Small:** Thanks for that, I mean I think we're starting to get some of the contours of what's
28 going on here and as you say, the question about what gets delivered direct to stores
29 versus what comes through the DC, that's obviously highly relevant.

30 I think, from my point of view, we seem to be moving part or very close to the end
31 of talking about feasibility, I think we understand that it's difficult and that there'd be a
32 number of things to work through and some of those things would have to be, Foodstuffs
33 at least are signalling that some of these things that they'd want to discuss in confidential
34 sessions, which is fine.

35 Before we move onto the question of how we go about it, which is the key thing I
36 want to cover next, which is voluntary undertakings or some kind of regulatory regime, I
37 will come to Josh for a comment and you might like to blend your comment into that next
38 session if you feel so inclined, Josh.

39 **Mr Gluckman:** Thank you Commissioner. I will attempt to blend. And while we didn't say much
40 before, that was because I think your summary of the Woolworths NZ position in our
41 submission was very accurate of us being open to voluntary wholesale supply, if

1 considered necessary over time. But there were a number of things that would need to
2 be worked through as you've outlined.

3 We think, you know, maybe the one topic that might merit a little bit more
4 discussion, but in the interests of time we could pick up in our confidential session, is the
5 dynamics of promotional funding that I think some of the other parties have touched on
6 because we do thing that's informative to how the mechanics of any supplier
7 arrangements might work.

8 And I might just briefly touch on private label insofar as, I guess in our view, and
9 obviously we've outlined that even though private labels are a relatively small part of our
10 business, its something that delivers a number of benefits, like with the low prices and
11 increased choice and innovation. So, I think you'd just want to be wary that any wholesale
12 solution didn't disincentivise development and innovation of private label products
13 because that wouldn't be a good thing for Kiwi customers.

14 But that said, if we were in the business of voluntary wholesale supply, we'd
15 absolutely be open to engagement with commercial customers on whether that's
16 something that was or wasn't included. And that's probably the point around private
17 label.

18 If I now attempt to blend in relation to the question around voluntary versus
19 regulated. Certainly we think that voluntary is a very, very sensible place to start and far
20 more likely to result in – if considered required, I should note, we don't think that
21 wholesale access is an essential but I think that's a given at this point – because voluntary
22 schemes are much more likely to result in more flexible and more efficient and more kind
23 of fit for purpose arrangements and the needs of a Night 'n Day would be very different
24 from the needs of a Supie would be different from the needs of a Warehouse, etc, and I
25 think that you know, thinking about how a regulated access regime, for example might
26 pick up all of those different permutations, I think it would be extremely complex. I mean
27 the types of issues that would need to be worked through and I think – because there's
28 not even an existing wholesale market where, you know, we're not a wholesaler, right,
29 we're a vertically integrated retailer, we buy and we sell and we operate as such. You're
30 not even taking an existing business model and kind of enshrining it with regulated
31 controls. You actually have to develop the thing from scratch and so that's complex and
32 highly likely to be rigid and inflexible and all of those types of things.

33 So I mean, you know, how would you regulate quality of supply between a brussels
34 sprout a or a brussels sprout b? How would you cover all of the different permutations for
35 different forecasting accountabilities, where different potential customers would have
36 very different requirements or capabilities. What benchmarks you'd use for fair and non-
37 discriminatory where there isn't an existing a wholesale model in place. You know,
38 different cost to serve parameters, a customer with 10,000 SKUs is going to have very
39 different cost to serve to one with 100 SKUs and you know, we don't even run cost to
40 serve models in our existing operation internally at the moment for our different
41 Countdowns, etc. So, you know, in terms of the capabilities.

1 The promotional or proportional allocation, how you deal with some of those
2 concepts, would it be a particularly in the case of supply shortages of which there
3 frequently are, you know, would that be based on size, would it be based on the
4 remoteness of a store, would it based on particular customer profile, you know, these are
5 traceability and recalls. I can go on, I guess my point is there's an inordinate number of
6 permutations that I think would be exceptionally complex and I think you'd be highly likely
7 to end up with a lot of inefficiencies and rigidity versus, you know, direct commercial
8 arrangements are a far more likely to achieve efficient results.

9 **Dr Small:** Thanks for that. So just while you're there though, could I ask you, I mean you have
10 almost exactly what you described, a direct commercial relationship in some kind of
11 wholesale type nature with Fresh Choice and Supervalu. And these are owner/operator
12 franchises obviously. In what way would that relationship be different do you think, to,
13 for example, supplying Night 'n Day. What would be the key differences from your point
14 of view in what you currently do with those franchisees compared to the way that you
15 envisage working with somebody else, even it wasn't Night 'n Day it might be, let's just
16 assume another store that looked more or less the same as a Supervalu or a Fresh
17 Choice?

18 **Mr Gluckman:** Thanks Commissioner. I think it's a good question because again maybe it's a bit
19 like the Foodstuffs example where from the outside there might be an assumption around
20 the way things have worked which is different to how they are.

21 **Dr Small:** Yeah, you've obviously figured something out that works.

22 **Mr Gluckman:** And so our franchise business and look, I'm happy to go into the gritty detail of all
23 of the ins and outs of that in kind of a one to one session. But you know, it's a franchise
24 operation, not a wholesale operation, right, and it's built on a very integrated set of terms
25 and it's got a lot of intricacies that I think are quite important and make it quite different
26 from a classic wholesale relationship.

27 Now, unfortunately, it does come with the name, which carries a lot of baggage, as
28 it is a complete misnomer as the Commission will identify, right, in terms of it being WDL,
29 but that's actually a relic of an organisational history of many decades ago. And so the
30 way to think about the model is it's more akin, I guess, an integrated model with a
31 complex set of terms, interdependencies, you know, obviously the franchisees have the
32 type of retail pricing freedoms that you'd expect them to have as a franchise model, but
33 you know, you've got brand services, you've got promotional services, you've got
34 operating standards, you've got a number of support services and more.

35 And so it's more akin to the way a McDonalds model would work, rather than
36 wholesale supply to a distant party.

37 **Dr Small:** Okay, thanks for that, so it's much more integrated than pure wholesale, I take that
38 point. Okay, so I think we're at the point where essentially, both of the, or all three of the
39 major networks have more or less said that wholesale access is feasible but complicated
40 and that if it was done, you'd prefer to do it voluntarily and I can certainly see that point.

1 I'd like to come to people who might want such access and ask them about how
2 would you feel, I guess, and how bankable would it be to leave this question of wholesale
3 access to commercial negotiations between yourselves and the majors? Tex Edwards has
4 got his hand up, comment on this?

5 **Mr Edwards:** Thank you Commissioner Small. We've seen this movie before. And thank you to
6 my industry colleague, Mr Quin, for just sharing the memory block I had about
7 telecommunications. Look last time we did one of these similar arrangements in the
8 telecommunication industry, we didn't have the beauty that we have today and the
9 beauty today is that we've got two like for like players in wholesale.

10 Last time when we had a negotiation like this, we had a GSM player and a TDMA
11 player. So the challenger could only negotiate with GSM. The challenger could only
12 negotiate with one party.

13 Here, game theory serves the position of the Commission, if there was to be an
14 unbundling of 150 supermarkets or a chunk of market share, then on a commercial basis,
15 both Boards of Countdown and the Board of Foodstuffs would want to capture that extra
16 reservoir of supply into their supply chain, because it gives them scale and knowledge and
17 it does give some benefits. I applaud the dialogue of Josh here and Jo Allan, thank you for
18 sharing with me the challenges that will have in the negotiation and cataloguing these
19 challenges for the transcripts. I found that useful.

20 I do close my comment about this type of negotiation. Of course we need a
21 regulatory backdrop, but on a game theory basis if we notice the difference we had in
22 Johannesburg as a third operator was GSM/GSM, in the previous telecommunications
23 industry we had GSM, TDMA, so the Commission actually had to pound the table and do a
24 war dance to get a GSM/GSM roaming agreement. Here we do have a minute commercial
25 interest if there was to be an unbundling of supermarkets in negotiating a voluntary
26 undertaking. Thank you.

27 **Dr Small:** Thanks for that, I mean that's obviously, that's predicated on doing something fairly
28 drastic at the retail space and we haven't quite got to that point in our conversation yet,
29 that's going to be on Monday. And I certainly take your point that in such a scenario yeah
30 there probably would be a desire to try and supply.

31 So perhaps my question is better directed at Sarah Balle and Matthew Lane, how
32 would you feel about going into voluntary negotiations with Foodstuffs or Woolworths or
33 perhaps they've both put their hands up for it and you could go and talk to both of them.
34 Matthew's got his hand up, how would you feel about that? No, Matthew's hand has
35 disappeared, Sarah's got her hand up.

36 **Ms Balle:** Sorry, I was going to say Matthew was on mute. Matthew do you want to go ahead
37 and then I'll follow you.

38 **Mr Lane:** My apologies. So look I think what we've heard in the last 30 minutes or so is that
39 extensive list of reasons why it can't be done and very little rationale in terms of why it
40 can be done. I think that summarises our frustration over the last 5 to 10-years with
41 grocery wholesale. There's a very strong preference there obviously to look after their

1 own banners and protect those own banners and look, I can fully appreciate that, I'd
2 probably want to do the same, don't get me wrong. But what it has done is it's prevented
3 anyone else growing in this industry. So where we can enter voluntary discussions are we
4 going to receive the same or better terms than Fresh Choice, Supervalu, On the Spot,
5 Four Square, PAK'nSAVE, New World, Countdown? Look I simply think we're not going to
6 and I think that ultimately means nothing changes. I believe there's no desire to chase our
7 business just despite the fact, you know, we're going to have 50 stores across the country,
8 we do have what some would call significant volume, just not when you compare it to the
9 two majors.

10 So yeah look, I'd probably battle with this voluntary one and I think that what it
11 does is it means that we should look at the separation of wholesale to retailers to actually
12 give the wholesalers determination to cover the whole market.

13 **Dr Small:** Thanks for that. Sarah don't feel you have to comment on this, but if you want to,
14 please.

15 **Ms Balle:** Yeah so, I probably have two points. So one is following on from Matthew's comment
16 around a split because I can't see how it would work if it was just a wholesaling part of
17 their organisation, it would need to be split.

18 But the other thing that I'm thinking is around some sort of regulation about that
19 we can access the same suppliers and the same products at a similar price level without
20 the fear of repercussions for the suppliers. Because that is definitely an issue. I can list
21 100s of products that we are not able to access because Foodstuffs and Woolworths have
22 exclusive supply arrangements and consumers demand those products and when we
23 don't have them, it makes competition really difficult for that main shop. So even if it
24 wasn't a, in terms of regulation, in terms of being able to get wholesale supply there then,
25 it's just the access to the products, the suppliers and the pricing from suppliers without
26 that fear of repercussion.

27 **Dr Small:** Okay, thanks for that. So your point you made there was about a kind of a separation
28 and it chimed for me with one of the things that Foodstuffs was saying about how you
29 don't have a separate wholesale function, you have to actually do this, have to create such
30 a thing. So I'm wondering whether that could be created in such a way that it was
31 conducive to this, it probably would be a specialised unit.

32 So that brings us to, I think, to the question about, so I think move on slightly down
33 the line here now, from voluntary towards perhaps the next step which might be some
34 kind of enforceable undertaking on the part of the major supermarkets to supply. So
35 could I just explore that with Chris Quin since you've got your hand up and feel free to
36 comment on what came before as well, Chris, at the same time.

37 **Mr Quin:** Thank you Commissioner. So I'll try and be quite brief. I think firstly, the point that's
38 been made a couple of times around trade terms versus volumetric terms really is quite
39 important to this conversation. Because the ability of regulation to deal with both those
40 dynamics is interesting and challenging.

1 Secondly, I think there's a fundamental difference between some of the different
2 industry models that have been given around telco in particular, or even fuel more
3 recently where there has been a single industry asset, whether that be a copper network,
4 a mobile network or a fuel supply chain, that can be regulated and then supply all, as
5 opposed to the business structure that we're talking about where we, as the retailer, are
6 an aggregator of thousands of suppliers' products.

7 And Commissioner, you mentioned the 32c, just a quick clarification, of the dollar
8 of retail, 19c is the retailer's component. Of the 32, 13 is GST. We don't have any say on
9 that one.

10 So the first difference, it's really important to think about and why we think
11 voluntary is appropriate is because there's not a natural monopoly asset or non-
12 substitutable product to regulate.

13 The other thing we'd say is that the barriers aren't getting access to land, they
14 aren't getting access to supply chain. There is differences potentially in what products can
15 be bought for by various parties, but that is potentially in the hands of suppliers as much
16 as it is in the hands of retailers. So when you think about regulation, what would be the
17 scope in terms of who would need to be captured to get the result?

18 Quick comment on private label. Look, we think there's just, you know, the
19 answer should be there's no basis to treat any company's private label product range
20 differently to any other suppliers. So should have normal commercial freedom to deal
21 with its customers and make its decisions based on what's appropriate.

22 It was mentioned that we don't use a retail brand on our private label. That's
23 cause we're a multi-brand retailer. So we had to have one that covered all of our brands,
24 quite simply, is the history of that particular issue.

25 So thank you, that was just a few comments I wanted to make, hope that helps.

26 **Dr Small:** Yeah it does help, thank you. So regarding voluntary supply and just sort of again,
27 pushing down the spectrum a little bit towards enforceable undertakings, could you
28 envisage a situation where you might – I think, certainly from what I've heard from
29 smaller operators in the room, is a kind of a, I guess, a fear of putting all their eggs in your
30 basket on a wholesale basis if it was purely voluntary. And I'm wondering whether you
31 could envisage a world where you give them some further assurances about how you
32 might conduct your voluntary relationship. So in some sectors people put up, for
33 example, an access charter and that would perhaps have some principles in there about
34 how you would deal with third parties. And I just sort of invite you to think about that and
35 whether that's much different to, that approach will be much different to an enforceable
36 undertaking in content in terms of what might, how it might be drafted and what it might
37 cover, obviously it will be different in terms of enforcement. But have you got any
38 thoughts on that sort of approach Chris?

39 **Mr Quin:** I don't have detailed thoughts Commissioner; we haven't done the assessment and the
40 preparation. I think it's important note that customer need and potential for whether we
41 can commercially meet that need, would be the critical thing to think about in voluntary.

1 So as we've said right at the beginning, understanding what customer, what demand,
2 what period of time, what volume, the service and support that is required, and then as
3 we do with many of our wholesale customers, deal in a very transparent way positioning
4 the service we could offer and the economics that makes sense for a fair return on the
5 capital invested in that part of the business.

6 And then, potentially being able to give suppliers more certainly about supply, so
7 maybe unlock more of that support and the ability to buy well to support those customers
8 could be part of the solution.

9 **Dr Small:** Thanks for that. Just on enforceable undertakings more generally, and this is open to
10 anybody, from any of the firms or any of the advisors. If such a regime was contemplated,
11 does anyone have views about how it should run, who should decide whether to accept
12 such a thing and what criteria should be used and any enforcement mechanisms? Andy
13 Mathews has got his hand up. He knows something about these things from Telco
14 probably, Andy can we hear from you?

15 **Mr Matthews:** Thanks Dr Small. Just hearing the discussion earlier, to me there are a couple of
16 points that the Commission's well aware of and in terms of these access issues it's sort of
17 about the ability and incentives and we're hearing with the current structure, it's very
18 hard, and I think that all makes sense.

19 But there is also the matter of incentives and I think that will apply to a voluntary
20 regime and potentially also an undertaking. I think that leads to your question, although
21 there's a related question as to why these things aren't being offered at the moment if
22 there is the demand. But park that.

23 So generally you need very similar concepts to what FGC were submitting in
24 relation to private label. Independent oversight is always going to be more powerful. An
25 access provider will always have incentives and there's nothing wrong with that and they
26 will see things in a particular way and an access seeker will see things in a particular way.
27 So there is a benefit in having that independence I think that independent oversight for
28 interpretation in dealing with disputes.

29 But a related thing is, and I don't know whether it's feasible here and it's not
30 necessarily what NZFGC are advocating for, but it does lend itself to structural separation
31 possibly with accounting separation. If there are these great difficulties in how you deal
32 with different offsetting mechanisms, if some of them relate to retail, then they should sit
33 in the retail function. And I think that's the thing we've seen with a lot of access regimes,
34 it's trying to work out where the profit margins are and that's what Chris Quin was really
35 saying too in terms of the return on assets in the wholesale function and I think everyone
36 would agree that that should earn its appropriate return. But by having structural
37 separation then it is easier to enforce those sorts of things. And again I'm not saying that
38 FGC are advocating for that, but that is one of the benefits that you have greater
39 transparency in terms of those sorts of equivalence or non-discrimination type
40 obligations.

1 **Dr Small:** Yeah, thanks for that. While you're there Andy, we've foreshadowed in the draft
2 report also considered access regulation. And so in that context and going to your
3 separation point, is some kind of operational separation effectively required for an
4 effective access regime, do you think? And would it be enough.

5 **Mr Matthews:** I think it's easier for transparency, I think if you have a non-discrimination
6 obligation, that can generally be quite soft and naturally an incumbent may want to
7 prioritise itself, which is understandable and normal and what you see as an access seeker
8 is a lot of non-price issues can be raised in terms of not providing service. So I think the
9 benefit in having some form of separation, can enable confidentiality, can enable greater
10 transparency and I'm sure the supermarket would say that there can be inefficiencies with
11 that too and it's a balancing of those factors and whether, I think Josh Gluckman said
12 earlier, he talked about removing double marginalisation. I don't know whether we've
13 seen evidence that that's the case, but if that's the case then it might mean that you need
14 full scale vertical integration. Either way it suggests to me that there's quite a barrier here
15 to overcome because it's either a barrier just getting wholesale access or you need to be a
16 fully vertically integrated player, whether its online or a mix of online and bricks and
17 mortar.

18 **Dr Small:** Right, thanks for that. Chris Quin you've got your hand up to react to some of that,
19 we're talking now about, I guess, about the trade-offs between these various ways of
20 arranging things. And you, from a telco background also have some experience of access
21 regulation, so have you got any thoughts on that that you'd like to share in terms of how, I
22 mean I think one of the things that is certainly on my mind is that given the complexity
23 and we certainly appreciate that there's a lot of cost in here, but given the complexity, it
24 seems that some kind of specialised wholesale function might be necessary and at that
25 point, if you're after non-discriminatory terms, is an access regime a good way to achieve
26 that?

27 **Mr Quin:** Thank you Commissioner. I wanted to maybe go back to two or three quick principles.

28 The first one is, there isn't a single asset or supply item to regulate. There is
29 thousands of supply items coming from hundreds if not thousands of suppliers. And that
30 is a fundamental difference between some of the other models the conversation is being
31 compared to. And I believe, potentially the appropriate equivalent of access regulation
32 and the concept of that in this market situation might well be the Code of Conduct.
33 Where we've already been clear in our action plan in our response to say, one of the key
34 things that should do is protect supplier freedom to supply any retailer. And I think that
35 part of it being clear in a Code of Conduct actually gives you the effect you're looking for
36 without some of the overload or risk or additional cost into an industry that has to do
37 everything it can to get prices down for consumers.

38 So, I think that's some way to think about it is that if that protection is very clear
39 and in place and there's been a few comments made about suppliers feeling like they
40 can't or are under pressure in some way to not supply. Look, I don't have current
41 examples or issues in front of me, we don't have specificity, but all I would say is where
42 absolutely said in the code, we should make that clear, and that it's administered well and
43 we've already covered that ground.

1 So, I think the supplier's ability to provide access to any retailer, can be captured
2 through that, thank you.

3 **Dr Small:** That's an interesting way to think about it, I appreciate the thought. So just following
4 that a little further, are you suggesting that. The code, as we saw it, was going to deal with
5 relationships between retailers and suppliers. It sounds as though what – I'm interested
6 to hear your elaboration on this as to how it would also solve an access problem. Because
7 does it mean, for example, does it bind suppliers to sell to other parties on the same terms
8 as they sell to you?

9 **Mr Quin:** I don't have a detailed answer, I haven't thought that through. I think you would want
10 to leave suppliers with their own commercial freedom. But what it would do is firstly deal
11 with the issue of any feeling that any one retailer could prohibit access to anyone else.
12 That clearly wouldn't be in the interests of competition and not in the interests of
13 customers. So I think it can certainly deal with that matter.

14 Then, you know, if we keep coming back to roughly for a \$1 of retail, 19c, that's
15 what the retailer, a portion was GST and a portion was supplier, in order to tackle this
16 issue that has been identified by multiple retailers, somehow the whole of the component
17 of cost needs to be thought about. But I haven't worked through in my mind, sorry
18 Commissioner, the thinking about whether it would go as far as that. But I think its an
19 important part of the conversation.

20 **Dr Small:** Yeah, okay thanks for that. We're getting close to the end here, I'll come to Matthew
21 Lane and then to Tim Donaldson and then to Nick Hogendijk.

22 **Mr Lane:** I just wanted to reiterate cause we are talking around voluntary and regulated
23 opportunities here and look why I appreciate that's certainly a step forward from where
24 we are currently. I think what we've highlighted here as well is around a conflicted
25 wholesale network. The data, you know, we would like to know what the Four Square 4
26 doors down from us was purchasing, what products were being purchased more than
27 others, what geographical regions of the country were performing better than others. We
28 have the opportunities to put new stores in based on where the centralisation of the
29 purchases are coming from.

30 So that being put aside that's just massively conflicted in any market you're trying
31 to make competitive. Ultimately you're creating a rod for your own back. And further to
32 that, it doesn't address the issue around the 80 or greater percent market share that
33 these two hold, what happens is, it just locks it in further for them. They centralise even
34 further buying power and can leverage suppliers even further through this model.

35 And I'll probably summarise it with the wholesale network that vertically
36 integrated definitely has its place, it has its place in Australia and it works well. But that's
37 when there's independence involved in the wholesale network that are competitive.
38 Without it any independence in the wholesale network, it is a duopoly, regardless if its
39 regulated or voluntary and it will continue to prevent entrants of scale further from
40 establishing as they haven't done for the last however many years.

1 So I think we've got to be careful here that just by opening it up, it's going to solve
2 the current pain point for existing retailers, like Supie and Night 'n Day, that we don't have
3 any security with it at the moment, but is it going to give an opportunity to grow and
4 establish market presence and drive down prices for consumers? And I just don't think a
5 conflicted wholesale network across two major retailers can do that.

6 **Dr Small:** Thanks for that Matthew, I noted you made that point a couple of times that one of
7 the disadvantages of wholesale access regimes is it does just keep the wholesaling
8 function to two, so thank you for that. Tim Donaldson.

9 **Mr Donaldson:** Thank you Commissioner. Look, as we've discussed, we're not currently
10 structured to enable separation. We're a fully integrated complex business. And this
11 structure isn't unique globally and for traditional retailers, it's actually the most effective.
12 For Foodstuffs SI this structure provides the most efficient supply chain which enables us
13 to deliver the best offer to the customer. And we haven't had a lot of discussion today
14 about the impact on the customer.

15 So, if we were to separate, we'd need to conduct significant analysis to understand
16 the implications including all of the unintended consequences of all the various scenarios.
17 And we need to determine the split of functions within each business valuations, the
18 ownership structures, and the additional resources to operate two separate business.

19 So, I just wanted to reinforce the fact that, you know, the term that the
20 Commission have used of vertical integration, is the most efficient way for retailers to
21 operate and we've heard from Supie today, that that's the track that they are going down.
22 So thank you.

23 **Dr Small:** Thanks for that, we haven't quite got to structural separation consideration yet but I
24 take your point. So Nick Hogendijk.

25 **Mr Hogendijk:** Yeah good afternoon. I'll keep it fairly short. Just as a precursor, to Jo Allan's
26 point about suppliers being requested to move stock into the DCs, we'll agree to disagree
27 cause I've got plenty of anecdotes that suggest – I also don't expect Jo or Chris or Dave to
28 actually have access to all those conversations that go on at levels below them.

29 Just simply from yesterday and today, it feels like we're getting conflicting
30 messages. Yesterday we heard supply chain was a challenge. Today we heard that the
31 supply chain is in abundance. There's 3PLs that are readily available, ambient and chilled.
32 We heard that its very price competitive and then we're hearing from people like
33 Matthew Lane today, and Sarah Balle from Supie, that the big two have a very clear gap in
34 pricing both access to and what they can deliver at the point of purchase.

35 There's significant cost impacts and there's negative impacts, there's a lot of,
36 almost overdriven the message around of there's a lot of complexity, there's a lot of need
37 to do a lot of homework and it feels like it's a little bit of passive scaremongering in terms
38 of, don't change, don't rock the boat.

39 The bottom line is and Dave McAuley from my team, who is on this call, who's ex-
40 Woolworths, ex-Metcash and has been involved in this industry for a long time, aptly put

1 earlier that independent wholesalers can't work without volume. Metcash proves the
2 model works and supports all different types of retailers. The simple message there is, it's
3 scale is the key and volume is the key. That is actually the critical message. To be able to
4 do that, you know, removing covenants and land banking if that's the case, using use or
5 lose approach to land that we were talking about earlier today, if you haven't used it for a
6 period of time, it's off your list, it has to go. Equalising purchase prices, these types of
7 things need to occur and realistically to do that independently probably requires the
8 Commission to go and look at three or four options, completely independent of the
9 competitors in the market space today and evaluate bottom up and top-down cost models
10 of those to see what truly works.

11 It's not to bust up Woolworths or Countdown. And a Code of Conduct, to Chris's
12 point, is part of the process here, but there's also risk associated with that because if you
13 say you can't supply brand exclusively to Chris's team, and you've got an agreement to
14 give him a controlled brand, that's actually counterproductive as well.

15 So, it's a very tight line that's got to be walked there, but in the submission we
16 make we'll recommend that you look at this independently of the competitors in the
17 marketplace and what some of the options are to come to the best solution for NZ
18 consumers.

19 **Dr Small:** Thanks Nick and remind us again we've still got another round of submissions and so I
20 hope that this conversation is stimulating thoughts for everybody, it certainly is for us. So
21 nearly at the end, Josh Gluckman, maybe final comment from you.

22 **Mr Gluckman:** Thank you Commissioner. I guess just to summarise our view on some of the
23 points recently made. At a 10,000-foot view we don't think wholesale access is necessary
24 or required. Like we're already seeing entry into the market occurring absent that. But if,
25 at the end of the market study process or if after some of the other changes that have
26 been proposed, you know, have had chance to take effect, there was a view that there
27 was wholesale access necessary, we think it would make a lot more sense to start at the
28 voluntary end of the spectrum and obviously we've got an open mind to doing that and
29 you know, while there would be some things to work through, we don't think it's
30 insurmountable and in our submission we also make that point. We'd be extremely
31 incentivised to make it work, you know, we understand the context of the market study,
32 we understand some of the more drastic options that have been entertained. And so if
33 we were going to invest and take the time to develop the capabilities to supply competitive
34 wholesale, we'd actually want to maximise the benefits from doing that. So we'd be very,
35 very incentivised to make it work.

36 We think that, you know, there's been a little bit of touching on this, I guess, the
37 telco analogy and structural separation. The more you separate the more inefficient you
38 become, the more inflexible you become, I'm not sure that, you know, open heart surgery
39 on the food supply chain is the best idea and so it would come with some risks. And
40 grocery retail certainly not telco. You know we've got tens of thousands of ever-changing
41 products. We've got these significant promotional funding pools at play. We've got, you
42 know, we don't have a monopoly. Worst case we have a fiercely competitive duopoly, but

1 even we don't support that characterisation. You know we've got very different capital
2 intensity of entry –

3 **Dr Small:** We appreciate this.

4 **Mr Gluckman:** - So I think that probably summarises our perspective, we think we'd be
5 incentivised to make it work if it was considered that that was something that was sought.

6 **Dr Small:** Thanks very much for that Josh. It's been a really fantastic conversation. Thanks to
7 you all, we're going to call it to a close there and we are going to be back on Monday for
8 the session on, which is more about separation actually, or actually it's about retail. So I
9 look forward to seeing you there and in the meantime have a happy and safe weekend,
10 thank you very much.

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