

## Statement of Issues

### Life Health Foods / Chalmers Organics

23 March 2022

#### Introduction

1. On 23 December 2021 the Commerce Commission registered an application (the Application) from Life Health Foods NZ Limited (Life Health Foods or the Applicant) seeking clearance to acquire 100 percent of the assets of Chalmers Organics Limited (Chalmers) (the Proposed Acquisition).<sup>1</sup>
2. To clear an application, the Commission must be satisfied that an acquisition would not have, or would not be likely to have, the effect of substantially lessening competition in a New Zealand market.
3. This Statement of Issues (Statement) sets out our concerns about the potential competition issues we have identified following our initial investigation. This is so Life Health Foods, Chalmers and other interested parties can provide us with submissions relating to those concerns.
4. In reaching the preliminary views set out in this Statement, we have considered information provided to date by the merging parties and other industry participants. We have not yet made any final decisions on the issues outlined below (or any other issues) and our views may change, and new competition issues may arise, as the investigation continues.

#### The concerns we are testing

5. We are still to conclude on the definition of the relevant markets. Our investigation is focusing on the product and customer dimension of the relevant markets.
6. At this stage, our primary concern is that the Proposed Acquisition could have the effect of substantially lessening competition due to horizontal unilateral effects<sup>2</sup> in a national market for the supply of tofu to the major grocery retailers.<sup>3</sup>

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<sup>1</sup> A public version of the Application is available on our website at: <http://www.comcom.govt.nz/business-competition/mergers-and-acquisitions/clearances/clearances-register/>.

<sup>2</sup> This refers to the merged entity's ability to profitably increase price beyond a competitive level or reduce non-price factors such as quality or innovation beyond a competitive level.

<sup>3</sup> Major grocery retailers are grocery retailers that operate a large number of supermarkets. The major grocery retailers in New Zealand are Woolworths New Zealand, Foodstuffs North Island, and Foodstuffs South Island. Woolworths NZ's retail banners are Countdown, FreshChoice and SuperValue; Foodstuffs

7. We explain our reasons for our preliminary view below and invite submissions on them.
8. Other than in the supply of tofu to the major grocery retailers, the merging parties overlap in the supply of other plant-based meat-alternative products, specifically, meat-alternative burger patties and meat-alternative sausages. However, we have fewer competition concerns arising as a result of the Proposed Acquisition in any of these areas. This is because the evidence to date indicates that the merged entity would be constrained by the presence of existing competitors who provide products that are close substitutes for those from the merged entity.
9. The merging parties also overlap in the supply of tofu to other customers. However, we have fewer competition concerns arising as a result of the Proposed Acquisition in this area. This is because the evidence to date indicates that the merged entity would be constrained by the presence of existing competitors who supply tofu to other specialty retailers, such as Asian supermarkets and vegetarian stores.
10. However, we are continuing to consider whether the Proposed Acquisition would have the effect of substantially lessening competition in a relevant market due to:
  - 10.1 horizontal unilateral effects in the supply of tofu to customers other than the major grocery retailers; and
  - 10.2 horizontal unilateral effects in the supply of plant-based meat-alternatives (excluding tofu) to any retail or wholesale customer.
11. At this stage, we do not have concerns about, and are planning no further investigation into, whether the Proposed Acquisition would substantially lessen competition in a relevant market due to:
  - 11.1 coordinated effects; or
  - 11.2 conglomerate effects.

## Process and timeline

12. We have agreed with Life Health Foods to an extension of time until **14 April 2022** in which to make a decision.
13. The Commission would like to receive submissions and supporting evidence from Life Health Foods, Chalmers and other interested parties on the issues raised in this Statement. We request responses by close of business on **4 April 2022**, including a public version of any submission.

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North Island's retail banners are PAK'nSAVE, New World, and Four Square.; Foodstuffs South Island's retail banners are PAK'nSAVE, New World, Four Square, Raeward Fresh, and On the Spot.

14. All submissions received will be published on our website with appropriate redactions. All parties will have the opportunity to cross-submit on the public versions of submissions from other parties by close of business on **11 April 2022**.
15. If you would like to make a submission but face difficulties in doing so within the timeframe, please ensure that you register your interest with the Commission at [registrar@comcom.govt.nz](mailto:registrar@comcom.govt.nz) so that we can work with you to accommodate your needs where possible.

## Industry background

16. The merging parties both supply a range of manufactured plant-based products. There is a growing range of plant-based products and all industry participants advised that the demand for these types of products, particularly those which are designed to be an alternative to meat, is growing rapidly. Whereas in the past these products appealed largely to dedicated vegetarian and/or vegan consumers, there is growing number of ‘flexitarian’<sup>4</sup> consumers who are looking to consume these products.<sup>5</sup> The different types of plant-based products currently available include:
  - 16.1 tofu;
  - 16.2 tempeh;
  - 16.3 meat-alternative patties;
  - 16.4 meat-alternative sausages; and
  - 16.5 meat-alternative chicken.
17. The plant-based products most relevant to this application are tofu, and meat-alternative patties and sausages, as these are the products which both merging parties supply (see Table 1 below).
  - 17.1 Tofu is made by coagulating soymilk and then pressing the resulting curds into solid white blocks of varying softness.<sup>6</sup> It is typically used as an ingredient as part of a meal. It can then be further processed – including flavouring or frying.
  - 17.2 Meat-alternative patties are designed to be a substitute for animal protein patties and can be made from a variety of ingredients – some are made from predominantly “whole” ingredients, like legumes or vegetables, while others are increasingly being made with textured vegetable proteins. Similarly, meat-alternative sausages are designed to look and cook like those made

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<sup>4</sup> Flexitarianism is a style of eating that encourages eating mostly plant-based foods while allowing meat and other animal products in moderation. It is more flexible than fully vegetarian diets.

<sup>5</sup> Commerce Commission interview with [redacted]. Commerce Commission Interview with [redacted]. Commerce Commission interview with [redacted]. Commerce Commission interview with [redacted].

<sup>6</sup> The Application at [5.13]. The softness of tofu depends on how much moisture is pressed out of it, for example, firm tofu is pressed more than silken tofu.

from meat. Again, meat-alternative sausages can be made from a variety of ingredients.

### The merging parties

18. Life Health Foods and Chalmers are two of the largest manufacturers of plant-based products.
- 18.1 Life Health Foods supplies its plant-based products under brand names including Bean Supreme, Alternative Meat Co. and Vegie Delights.
- 18.2 Chalmers supplies its plant-based products under the brand names Tonzu and Zenzo.
- 18.3 The table below outlines the products supplied by Life Health Foods and Chalmers.

**Table 1: plant-based products supplied by Life Health Foods and Chalmers**

Product	Life Health Foods	Chalmers
Tofu	✓	✓
Tempeh	-	✓
Meat-alternative patties	✓	✓
Meat-alternative sausages	✓	✓
Meat-alternative mince	✓	-
Falafel	✓	-
Jackfruit	✓	-
Meat free 'chicken'	✓	-
Meat free 'bacon'	✓	-

Source: Application

19. Life Health Foods and Chalmers, as well as other suppliers of plant-based products, supply their products to consumers through a range of different wholesale and retail customers, although the extent to which each supplier uses particular wholesalers and retailers to supply end-consumers varies. The merged entity would supply product to:
- 19.1 the major grocery retailers;
- 19.2 specialty food retailers as well as Asian supermarkets;
- 19.3 food service providers such as small cafes and restaurants; and
- 19.4 home delivery service providers.<sup>7</sup>

### The relevant markets

20. We define markets in the way that we consider best isolates the key competition issues that arise from a merger. In many cases this may not require us to precisely

<sup>7</sup> These sales are usually made as a part of meal kits, such as My Food Bag.

define the boundaries of a market. What matters is that we consider all relevant competitive constraints, and the extent of those constraints. For that reason, we also consider products and services that fall outside the market, but which still impose some degree of competitive constraint on the merged entity.

21. When assessing relevant markets, we consider whether, in response to a price increase on products of interest by the merged entity:
  - 21.1 customers could easily switch to alternative products (known as ‘demand-side’ substitution); and
  - 21.2 suppliers of different products could easily, profitably and quickly switch to supplying the products of interest (known as ‘supply-side’ substitution).

### **The Applicant’s view of the markets**

22. Life Health Foods and Chalmers both manufacture plant-based products. Life Health Foods submitted that there is a single national market for the wholesale supply of all meat-alternative products, which it considered included all of the products listed in Table 1.<sup>8</sup> Life Health Foods submitted that:
  - 22.1 All the major suppliers of plant-based meat-alternatives distribute their products nationally to wholesale customers such as the major grocery retailers, specialty retailers, home delivery providers, cafes and restaurants.<sup>9</sup>
  - 22.2 All customers have similar requirements in terms of packaging and supply, and all suppliers could readily supply all customers.<sup>10</sup>
  - 22.3 All plant-based meat-alternatives – such as mince, patties, sausages, tofu and tempeh – are substitutes for most end consumers who buy any of them.<sup>11</sup>
  - 22.4 The same equipment can be used to manufacture a range of different meat-alternative products, and there are no significant barriers to switching production between types.<sup>12</sup>

### **Our preliminary views of the relevant markets**

23. We have not yet formed a final view on market definition. Our current view is that, while the relevant markets are likely to be for wholesale supply on a national basis, as the Applicant contends, it is also likely to be appropriate to use narrower customer and product markets to assess the impacts of the Proposed Acquisition. As

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<sup>8</sup> The Application at [5.30].

<sup>9</sup> The Application at [5.38].

<sup>10</sup> The Application at [5.44].

<sup>11</sup> For example, the Applicant provided market research that it says demonstrates that end-customers consume both tofu and other plant-based proteins in their diets. This, it says, is evidence that consumers consider tofu to be a substitute for other plant-based proteins. [ ] provided in Email from MinterEllisonRuddWatts (on behalf of Life Health Foods) to the Commerce Commission (7 March 2022); and The Application at [5.33].

<sup>12</sup> The Application at [5.34].

we explain further below, we currently consider that for both tofu and other meat-alternatives the major grocery retailers could fall within a separate customer market to other customers. We also consider, on balance, that tofu is likely to be in a separate product market to other meat-alternative products, although the evidence currently before us is less conclusive on this point.

### *Product Dimension*

24. At this stage, we consider that there are likely to be separate product markets for the supply of tofu and for other meat-alternative products.

### Demand side

25. On the demand side, we have heard mixed evidence about how end consumers (shoppers and diners) buy and consume plant-based products.
26. Some parties we spoke to believe that some consumers who buy these products see all of them as being broadly substitutable “meal solutions”, for example where a family member chooses not to eat meat.<sup>13</sup> The Applicant also provided market research indicating that many consumers eat multiple types of plant-based products, and submitted that this demonstrates that consumers may see the products as substitutes.<sup>14</sup>
27. However, we currently consider that, for many consumers, tofu may not be a close substitute for products such as meat-alternative patties and sausages.<sup>15</sup>
- 27.1 While meat-alternative patties and sausages are commonly consumed whole (for example, can be served in buns as part of simple meals or at barbecues) tofu is more often used as an ingredient in meals which require more mixing and cooking.<sup>16</sup>
- 27.2 While it may be possible to use firm tofu as a substitute for meat-alternative patties or sausages in a simple meal or at a barbecue (or to substitute between patties and sausages), it would not be realistic to use softer or silken tofu. It is also less likely that meat-alternative patties or sausages could be used instead of any type of tofu in a traditional Asian meal.<sup>17</sup>
- 27.3 In our view, the market research provided by the Applicant does not necessarily demonstrate that different types of plant-based products meat-alternative (for example, tofu, patties and sausages) are substitutes for each other. This research, which showed that consumers often eat several types of plant-based products, does not indicate whether consumers switch between

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<sup>13</sup> Commerce Commission interview with [ ].

<sup>14</sup> Email from MinterEllisonRuddWatts (on behalf of Life Health Foods) to the Commerce Commission (7 March 2022).

<sup>15</sup> Commerce Commission interview with [ ].

<sup>16</sup> Commerce Commission interview with [ ].

<sup>17</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

the different products, for example in response to changes in their relative prices.

- 27.4 The fact that consumers tend to buy tofu, as well as meat-alternative patties or sausages, may indicate that they are complements rather than substitutes. That is, consumers who eat plant-based products may want to eat a range of them but may only use one type for particular meals. For example, people who regularly cook Asian food (with or without meat) may use tofu, but may not switch to meat-alternative patties and sausages if the price of tofu increased significantly.
- 27.5 Market participants have also told us that consumer preferences for plant-based products are complex and, in some areas, fast-changing.<sup>18</sup>
28. On the basis of our investigation so far, we are not currently satisfied that different types of plant-based products (for example, tofu, patties and sausages) are substitutes for each other from customers' point of view.
29. We seek further submissions on the substitutability between different types of plant-based products, in particular in relation to which product(s) can be used as substitutes for tofu.

### Supply side

30. On the supply side, the evidence currently before us suggests that many suppliers would be able to switch production between meat-alternative patties and meat-alternative sausages. However, it also appears that most suppliers cannot easily switch production between these products and tofu.
- 30.1 Meat-alternative patties and sausages can be made with similar equipment, processes and ingredients.<sup>19</sup> On the other hand, tofu uses different equipment, processes and ingredients.
- 30.1.1 Tofu uses soybeans as its main input, whereas other plant-based products can use a variety of inputs. The main step in tofu production is coagulation, whereas some other plant-based products utilize more complex techniques such as fermentation.<sup>20</sup>
- 30.2 Suppliers that we have spoken with said they could not quickly or easily switch between making tofu and the other products. Rather, they said they would have to make significant investments in new capital, processes and

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<sup>18</sup> See, for example, Commerce Commission interviews with [ ], [ ], [ ], [ ], [ ].

<sup>19</sup> Commerce Commission interview with [ ].

<sup>20</sup> Commerce Commission interview with [ ].

staff to switch production either way, as any other new entrant would have to.<sup>21</sup>

### Preliminary conclusion on product markets

31. While it is possible that some consumers may see tofu and other meat-alternatives as being substitutable to a degree, the current evidence indicates that they are not closely substitutable on the demand or supply sides, and vice versa.

### *Functional dimension*

32. Since suppliers supply wholesale customers, and not end consumers, consistent with the Application, we consider that the functional dimension of the relevant markets is the manufacturer and wholesale supply dimension.<sup>22</sup>

### *Geographic Dimension*

33. At this stage, we consider that the relevant markets are likely to be national. The evidence suggests that the merging parties supply all customers on a national basis from central distribution bases.<sup>23</sup>
34. However, we are aware of a handful of smaller suppliers who consider they can only profitably supply specific regions, and who appear unable to expand to supply major grocery retailers nationwide, citing that the cost for chilled logistics can be prohibitive.<sup>24</sup> We continue to investigate whether it may be appropriate for us to define narrower geographic markets to assess the merger's impact in some areas.
35. We seek submissions on the appropriate geographic scope of the relevant market(s), in particular in relation to the supply of tofu.

### *Customer dimension*

36. The merging parties and other suppliers of tofu and meat-alternative products supply customers that are differentiated by size, with major grocery retailers at one end of the spectrum and smaller foodservice customers at the other.
37. We currently consider that competition to supply major grocery retailers should be assessed separately from competition to supply all other customers such as specialty retail stores (for example health food stores and speciality Asian supermarkets), foodservice providers (for example wholesalers to small cafes and restaurants) and home delivery service providers.

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<sup>21</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ]; Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>22</sup> The Application at [5.37]-[5.39].

<sup>23</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>24</sup> Commerce Commission interview with [ ]. Commerce Commission interview with [ ].



38. Based on the evidence gathered to date, it appears that the major grocery retailers typically place more stringent requirements on suppliers, and demand an expanded range of products (eg, different pack sizes, flavours) than other customer types do, and that only some current suppliers of tofu and meat-alternatives can meet all such requirements.
39. For example, as the major grocery retailers are trying to grow the category,<sup>25</sup> they may demand particularly high quantities and require fast turnaround times, and it appears that only some suppliers have the manufacturing and distribution capabilities required.<sup>26</sup> The major grocery retailers also sometimes impose additional conditions that only some suppliers can meet profitably.<sup>27</sup>
40. In contrast, it appears that foodservice and specialty stores typically apply lower requirements on suppliers compared to major grocery retailers, meaning that more suppliers can supply them.
41. There is little differentiation within the tofu and meat-alternative products that suppliers supply to each customer. For example, the same product sizes, in similar pack sizes, are supplied by the merging parties to both major grocery retailers and to foodservice customers<sup>28</sup>. However, as set out earlier, requirements of some customers do appear to vary, particularly to smaller suppliers.
42. We therefore currently consider that it is appropriate to consider the major grocery retailers to be in a distinct market from all other customers, particularly, because it appears that they have fewer options than specialty retailers.
43. We seek submissions on whether separate markets should be defined for major grocery retailers, in particular in relation to the supply of tofu.

#### **Preliminary assessment of the relevant markets**

44. On the basis of the above, we currently consider that there are separate national markets for the manufacture/importation and wholesale supply of:
- 44.1 tofu to major grocery retailers;
- 44.2 tofu to specialty retail stores, foodservice customers and home delivery providers;
- 44.3 plant-based meat-alternatives (excluding tofu) to major grocery retailers; and

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<sup>25</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>26</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>27</sup> For example, supermarkets sometimes require suppliers to help fund promotional offers, which can reduce suppliers' margins. Commerce Commission interview with [ ]. Commerce Commission interview with [ ].

<sup>28</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

- 44.4 plant-based meat-alternatives (excluding tofu) to specialty retail stores, foodservice customers and home delivery.
45. We seek submissions on our current views of the relevant markets.

### **With and without scenarios**

46. Assessing whether a substantial lessening of competition is likely requires us to:
- 46.1 compare the likely state of competition if the Proposed Acquisition proceeds (the scenario with the merger, often referred to as the factual) with the likely state of competition if it does not (the scenario without the merger, often referred to as the counterfactual); and
- 46.2 to determine whether competition is likely to be substantially lessened by comparing those scenarios.
47. With the Proposed Acquisition, Life Health Foods would acquire the business and assets of Chalmers. The Applicant has submitted that the most likely counterfactual is a continuation of the status quo. The Applicant also understands that Chalmers has limited potential for expansion with its current resourcing.<sup>29</sup>
48. At this stage, it appears that the status quo would be the most appropriate without the merger scenario, with Chalmers continuing to operate independently of Life Health Foods.

### **Competition assessment: unilateral effects – tofu markets**

49. Horizontal unilateral effects arise when a firm merges with or acquires a competitor that would otherwise provide a significant competitive constraint (particularly relative to remaining competitors) such that a market participant can profitably increase prices above (and/or reduce quality below) the level that would prevail without the merger.
50. In markets where products differ slightly from one another (known as ‘differentiated markets’), some products will be closer substitutes and compete more vigorously with each other than others. Unilateral effects are therefore more likely to arise where the products produced by the merging parties are relatively similar.
51. For the reasons set out below, we are currently satisfied that the Proposed Acquisition would not be likely to substantially lessen competition in the supply of tofu to specialty retail stores, foodservice customers and home delivery providers. This is primarily because, while both Life Health Foods and Chalmers supply tofu to some of these speciality customers, our preliminary investigation indicates there are several other suppliers of tofu who, collectively, would likely provide a constraint on the merged entity.

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<sup>29</sup> The Application at [3.7]-[3.8].

52. However, this does not appear to be the case when we have considered the supply of tofu to the major grocery retailers. For the reasons set out below, we are not currently satisfied that the Proposed Acquisition would not be likely to substantially lessen competition in the market for the supply of tofu to the major grocery retailers.

### **Applicant's submission**

53. Life Health Foods submitted that the Proposed Acquisition would not be likely to substantially lessen competition in any relevant market(s) due to unilateral effects because:<sup>30</sup>
- 53.1 tofu completes closely with all other plant-based products such as meat-alternative burger patties and meat-alternative sausages;
  - 53.2 the merged entity would face vigorous competition in the supply of tofu from all existing meat-alternative suppliers;
  - 53.3 barriers to entry and expansion to tofu and meat-alternative products are low;
  - 53.4 tofu can be easily imported meaning that the merged entity would be constrained by suppliers based overseas, as well as those based in New Zealand; and
  - 53.5 the major supermarket retailers would have countervailing power through an ability to expand their range of private label products, reducing shelf space to alternative suppliers and/or sponsor the expansion of an existing competitor.<sup>31</sup>

### **The market for the supply of tofu to the major grocery retailers**

54. At this stage, the evidence we have seen indicates that Life Health Foods and Chalmers are the two largest suppliers of tofu to the major grocery retailers and there appear to be less tofu suppliers who can supply those retailers than there are for all other customers.
55. For the reasons set out below, we are not currently satisfied that the Proposed Acquisition would not be likely to substantially lessen competition for the supply of tofu to the major grocery retailers.

### *The merging parties appear to be each other's closest competitor*

56. The evidence currently before us indicates that Life Health Foods and Chalmers are each other's closest competitor for the supply of tofu to the major grocery retailers. This competition would be lost as a result of the Proposed Acquisition.

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<sup>30</sup> The Application at [6.1 (a)-(d)].

<sup>31</sup> The Application at [6.42].

- 56.1 The Applicant estimates that Life Health Foods and Chalmers would account for in excess of [ ] of all sales of tofu by the major grocery retailers.<sup>32</sup>
- 56.2 In many parts of the country, the merging parties' products are the only brands stocked in the major grocery retailers.<sup>33</sup>
- 56.3 Whereas some tofu suppliers only supply one style of tofu into the major grocery retailers (eg, unflavoured – firm or silken), both Life Health Foods and Chalmers supply an expanded range of tofu products (including different flavours and pack sizes) in comparison to their competitors.
57. We invite submissions on how closely Life Health Foods and Chalmers compete to supply tofu to the major grocery retailers.

*Constraint from existing suppliers of tofu*

58. Our enquiries to date indicate that some competing suppliers are only currently servicing major grocery retailers in certain geographic areas. This is because:
- 58.1 small suppliers face higher logistics costs than larger suppliers, meaning they are less price competitive when supplying customers outside their region or on a national basis; and
- 58.2 smaller suppliers tend to have a more limited range of products. The evidence suggests that it would take significant investment and improved brand equity for them to increase their range to the point where they are desired by the major grocery retailers.
59. Additionally, since these suppliers only currently service smaller areas, they do not manufacture tofu on the same scale as the merging parties. This means that they often pay a higher unit price for key ingredients such as soybeans, which in turn, makes their margins thinner, making expansion more difficult.<sup>34</sup>
60. Given this feedback, we are not currently satisfied that competition from existing suppliers of tofu would provide sufficient constraint on the merged entity in supplying tofu to the major grocery retailers.
61. We invite submissions on the extent to which existing suppliers of tofu would impose a competitive constraint on the merged entity in the supply of tofu to the major grocery retailers.

*Constraint from new entry and expansion appears unlikely*

62. Entry or expansion must be likely, as well as timely, before it could constrain the merged firm and prevent a substantial lessening of competition. The likelihood of

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<sup>32</sup> The Application at [6.22]

<sup>33</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>34</sup> Commerce Commission interview with [ ].

entry or expansion depends on whether firms can profitably enter or expand in the market.

63. The evidence before us suggests that many tofu manufacturers who only supply tofu into specialty stores would face the same issues as the smaller suppliers to the major grocery retailers do when it comes to supplying the major grocery retailers and achieving ranging.<sup>35</sup>
64. As noted earlier, the requirements to manufacture tofu appear to be significantly different than those required to produce meat-alternative patties and sausages.
65. We received feedback from suppliers of meat-alternative products indicating that they would be unlikely to start manufacturing of tofu in response to an increase in the price of tofu.<sup>36</sup> Suppliers noted that in a small category like tofu, scale is very important, and competing with the merging parties would be difficult as they are the market leaders in tofu. Suppliers also noted that the returns on the level of capital investment needed to achieve ranging in major grocery retailers are unlikely to make such investment commercially attractive.
66. We are also continuing to assess the ability to import tofu into New Zealand. At this stage, we are not aware of any overseas-based tofu manufacturer that is routinely, and in sufficient quantities, importing tofu into New Zealand under its own label.
- 66.1 Initial enquiries indicate that overseas suppliers may be unwilling to supply their brands into New Zealand. We have received feedback that the strength of the current suppliers in New Zealand, the costs to develop the necessary brand presence in New Zealand, as well as the additional transportation cost, would make any entry via imports highly unlikely.<sup>37</sup>
67. We invite submissions on the extent to which expansion from manufacturers of other meat-alternative products and/or imports would be likely to effectively constrain the merged entity in the supply of tofu to the major grocery retailers.

#### *Countervailing power of major grocery retailers*

68. We are continuing to assess the extent to which a major grocery retailer might have countervailing power to constrain a price increase from the merged entity, including the ability to sponsor entry or punish the merged entity in another market, because at this stage, we are not satisfied that countervailing power of the major grocery retailers would be sufficient to constrain the merged entity.
69. The Applicant submitted that:
- 69.1 the merging parties' primary customers in the retail market are the major grocery retailers, and that the Commission has previously accepted that

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<sup>35</sup> Commerce Commission interview with [ ].

<sup>36</sup> Commerce Commission interview with [ ]. Commerce Commission interview with [ ].

<sup>37</sup> Email from [ ] to the Commerce Commission (2 March 2022).

major grocery retailers have strong bargaining power vis-à-vis their suppliers;<sup>38</sup>

69.2 post-acquisition, the major grocery retailers will continue to wield a considerable degree of countervailing power and impose a significant competitive constraint on the merged entity, through:<sup>39</sup>

69.2.1 introducing new, or expanding supply of, private label products;

69.2.2 sponsoring the expansion of a current competitor, or the entry of a new competitor, into the retail market;

69.2.3 reducing shelf space or promotional slots, or deleting SKUs; and/or

69.2.4 parallel importing other brands.

70. In terms of sponsoring new entry, as noted above, we have received evidence that there are challenges to importing tofu into New Zealand at a cost that allow suppliers to compete on price.

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71. We also note that Life Health Foods, and its associated companies, produce a number of products other than tofu (including meat-alternative sausages and patties, but also Weet-Bix and Marmite) which are sold through the major grocery retailers. We are considering the extent to which these retailers could respond to a tofu price increase in other ways, including whether broader relationships with the supplier may affect this.<sup>40</sup>

72. Finally, we are also considering the extent to which the major grocery retailers could expand their private label offering for tofu, for example by offering additional flavours or types, and whether this would sufficiently constrain the merged entity.

73. We invite submissions on whether major grocery retailers are likely to constrain a tofu price increase in any of the ways outlined above, or in any other ways.

*Summary of our current views on unilateral effects in the market for the supply of tofu to the major grocery retailers*

74. Based on the evidence gathered to date, we are not satisfied that existing suppliers of tofu would provide sufficient constraint on the merged entity to replace the competition lost as a result of the Proposed Acquisition.

75. Further, at this stage, we have not been able to identify a potential entrant who would be able to sufficiently constrain the merged entity. Expansion from existing

<sup>38</sup> The Application at [6.41]-[6.42].

<sup>39</sup> The Application at [6.43].

<sup>40</sup> Life Health Foods is owned by the same parent company as Sanitarium.

meat-alternative suppliers seems unlikely due to investment costs and relatively low margins without having the scale of the merging parties.

76. We are not satisfied that the major grocery retailers would be likely to exercise countervailing power in a way that constrains the merged entity.

### **The market for the supply of tofu to speciality retailers**

77. At this stage, our preliminary investigation indicates that, in addition to Life Health Foods and Chalmers, there are several other main suppliers of tofu to speciality retailers, foodservice customers and home delivery providers.
- 77.1 There appear to be less onerous distribution requirements for tofu suppliers, making it easier to maintain a presence in these areas.
- 77.2 While not all tofu manufacturers have national reach, the evidence indicates that all regions are served by several suppliers that would provide significant competition to the merged entity.<sup>41</sup>
- 77.3 None of the existing suppliers of tofu considered there are any significant constraints on their ability to expand their existing supply of tofu to speciality retailers.<sup>42</sup>
78. Based on the above, at this stage we are currently satisfied that the Proposed Acquisition would not be likely to substantially lessen competition for the supply of tofu to specialty retail stores, foodservice customers and home delivery providers.

### **Competition assessment: unilateral effects – meat-alternative markets**

79. At this stage, based on the evidence gathered to date, we consider that the merged entity would likely be constrained by the presence of several existing competitors, with the ability to expand, if there are national markets for the supply of:
- 79.1 meat-alternatives (excluding tofu) to the major grocery retailers; and
- 79.2 meat-alternatives (excluding tofu) to speciality retailers.
80. Industry participants advised that the demand for plant-based meat-alternative has been growing rapidly recently. Whereas in the past, plant-based meat-alternatives appealed largely to dedicated vegetarian and/or vegan consumers, there was a growing number of 'flexitarian' consumers who were looking to consume meat-

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<sup>41</sup> For example, although Chalmers is able to supply its tofu on a nationwide basis, it is not a leading supplier into specialty stores. On the other hand, local tofu suppliers are able to build relationships with local retailers on a store-by-store basis.

<sup>42</sup> For example, see Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

alternatives such as plant-based alternative meat patties, plant-based sausage alternatives and plant-based chicken alternatives.<sup>43</sup>

81. In turn, this has led to a growing number of meat-alternative manufacturers supplying a range of meat-alternatives. None of the existing suppliers considered there are any significant constraints on their ability to expand their existing supply of meat-alternative products.<sup>44</sup>
82. Accordingly, we are currently satisfied that the Proposed Acquisition will not have, or would not be likely to have, the effect of substantially lessen competition if there are markets for the supply of plant-based meat-alternatives (excluding tofu) to the major grocery retailers or to speciality retailers.
83. However, as indicated above in the market definition section, we are continuing to assess the constraint that plant-based meat-alternatives would place on the demand and/or supply of tofu.
84. We invite submissions on the extent to which the supply of plant-based meat-alternatives would impose a competitive constraint on the merged entity in the supply of tofu to the major grocery retailers.

### Next steps in our investigation

85. The Commission is currently scheduled to make a decision on whether or not to give clearance to the proposed acquisition by **14 April 2022**. However, this date may change as our investigation progresses.<sup>45</sup> In particular, if we need to test and consider the issues identified above further, the decision date is likely to extend.
86. As part of our investigation, we will continue to identify and contact parties that we consider will be able to help us assess the issues identified above.

### Making a submission

87. We are continuing to undertake inquiries and seek information from industry participants about the impact of the Proposed Acquisition. We welcome any further evidence and other relevant information and documents that Life Health Foods or any interested parties are able to provide regarding the issues identified in this Statement.

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<sup>43</sup> This sentiment was echoed by many industry participants, see Commerce Commission interview with [ ]; Commerce Commission interview with [ ]; Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>44</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>45</sup> The Commission maintains a clearance register on our website at <http://www.comcom.govt.nz/clearances-register/> where we update any changes to our deadlines and provide relevant documents.



88. If you wish to make a submission, please send it to us at [registrar@comcom.govt.nz](mailto:registrar@comcom.govt.nz) with the reference 'Life Health Foods/Chalmers' in the subject line of your email. Please do so by close of business on **4 April 2022**.
89. All information we receive is subject to the Official Information Act 1982 (OIA), under which there is a principle of availability. We recognise, however, that there may be good reason to withhold certain information contained in a submission under the OIA, for example in circumstances where disclosure would be likely to unreasonably prejudice the commercial position of the supplier or subject of the information.