

## Determination

### Life Health Foods NZ Limited and Chalmers Organics Limited [2022] NZCC 21

<b>The Commission:</b>	Anna Rawlings Dr John Small Elisabeth Welson
<b>Summary of application:</b>	An application from Life Health Foods NZ Limited seeking clearance to acquire the business and assets of Chalmers Organics Limited.
<b>Determination:</b>	Under section 66(3)(a) of the Commerce Act 1986, the Commerce Commission gives clearance to the proposed acquisition.
<b>Date of determination:</b>	26 May 2022

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## Contents

<b>CONTENTS</b> .....	<b>3</b>
<b>THE PROPOSED ACQUISITION</b> .....	<b>4</b>
<b>OUR DECISION</b> .....	<b>4</b>
<b>OUR FRAMEWORK</b> .....	<b>4</b>
<b>THE KEY PARTIES AND THE SUPPLY OF PLANT-BASED PRODUCTS</b> .....	<b>5</b>
<b>MARKET DEFINITION</b> .....	<b>7</b>
<b>PRODUCT DIMENSION</b> .....	<b>8</b>
<i>What Life Health Foods submitted</i> .....	<b>8</b>
<i>The Commission's view</i> .....	<b>8</b>
<b>CUSTOMER DIMENSION</b> .....	<b>10</b>
<i>What Life Health Foods submitted</i> .....	<b>10</b>
<i>The Commission's view</i> .....	<b>10</b>
<b>OTHER MARKET DIMENSIONS</b> .....	<b>11</b>
<b>CONCLUSION ON APPROACH TO MARKET DEFINITION</b> .....	<b>12</b>
<b>WITH AND WITHOUT SCENARIOS</b> .....	<b>12</b>
<b>HOW THE PROPOSED ACQUISITION COULD SUBSTANTIALLY LESSEN COMPETITION</b> .....	<b>13</b>
<b>COMPETITION ASSESSMENT – THE MEAT-ALTERNATIVE MARKETS</b> .....	<b>13</b>
<b>UNILATERAL EFFECTS IN THE MARKET FOR THE SUPPLY OF MEAT-ALTERNATIVES TO SPECIALITY CUSTOMERS</b> .....	<b>13</b>
<b>COORDINATED EFFECTS IN THE MARKET FOR THE SUPPLY OF MEAT-ALTERNATIVES TO SPECIALITY CUSTOMERS</b> .....	<b>14</b>
<b>UNILATERAL EFFECTS IN THE MARKET FOR THE SUPPLY OF MEAT-ALTERNATIVES TO THE MAJOR GROCERY RETAILERS</b> .....	<b>14</b>
<b>COORDINATED EFFECTS IN THE MARKET FOR THE SUPPLY OF MEAT-ALTERNATIVES TO THE MAJOR GROCERY RETAILERS</b> .....	<b>15</b>
<b>COMPETITION ASSESSMENT – THE TOFU MARKETS</b> .....	<b>16</b>
<b>THE APPLICANT'S SUBMISSIONS ON THE SUPPLY OF TOFU</b> .....	<b>16</b>
<b>UNILATERAL EFFECTS IN THE MARKET FOR THE SUPPLY OF TOFU TO SPECIALITY CUSTOMERS</b> .....	<b>16</b>
<b>COORDINATED EFFECTS IN THE MARKET FOR THE SUPPLY OF TOFU TO SPECIALITY CUSTOMERS</b> .....	<b>17</b>
<b>UNILATERAL EFFECTS IN THE MARKET FOR THE SUPPLY OF TOFU TO THE MAJOR GROCERY RETAILERS</b> .....	<b>17</b>
<i>Life Health Foods and Chalmers are each other's closest competitor in supplying tofu to the major grocery retailers</i> .....	<b>18</b>
<i>Constraint from existing competition in supplying tofu to the major grocery retailers</i> .....	<b>18</b>
<i>Countervailing buyer power of the major grocery retailers</i> .....	<b>19</b>
<b>COORDINATED EFFECTS IN THE MARKET FOR THE SUPPLY OF TOFU TO THE MAJOR GROCERY RETAILERS</b> .....	<b>21</b>
<b>CONGLOMERATE EFFECTS</b> .....	<b>22</b>
<b>OVERALL CONCLUSION</b> .....	<b>22</b>
<b>DETERMINATION ON NOTICE OF CLEARANCE</b> .....	<b>23</b>
<b>ATTACHMENT: MARKET SHARE ESTIMATES</b> .....	<b>24</b>

## The proposed acquisition

1. On 23 December 2021, the Commerce Commission registered an application (the Application) from Life Health Foods NZ Limited (Life Health Foods) seeking clearance to acquire the business and assets of Chalmers Organics Limited (Chalmers) (the Proposed Acquisition).

## Our decision

2. The Commission gives clearance to the Proposed Acquisition as we are satisfied that it will not have, or would not be likely to have, the effect of substantially lessening competition in any market in New Zealand.
3. Life Health Foods and Chalmers are two of the largest manufacturers of plant-based food products in New Zealand. The Commission's investigation focused on the potential for the Proposed Acquisition to have unilateral effects in the supply of tofu to the major grocery retailers<sup>1</sup> as this is where the merging parties most closely compete with one another.
4. The Commission found that most tofu sold in New Zealand is sold through the major grocery retailers. This is supplied as branded tofu by the merging parties and several other smaller suppliers, and as private label tofu by the major grocery retailers. The smaller suppliers are currently constrained in their ability to expand their supply to the major grocery retailers but could expand relatively easily if encouraged to do so by those retailers.
5. In this regard, the major grocery retailers have significant buyer power in their dealings with suppliers of tofu which they could use to constrain the merged entity by credibly threatening to promote the expansion of existing small suppliers or expanding production of private label tofu. We are satisfied that this countervailing buyer power would prevent the exercise of unilateral market power by the merged entity.
6. We also considered the potential for the Proposed Acquisition to result in coordinated effects and in conglomerate effects but consider these effects are unlikely. This is because the merger is unlikely to make coordination more likely, complete or sustainable, nor will it increase the merged firm's ability to foreclose competitors in any market due to bundling or tying.

## Our framework

7. Our approach to analysing the competition effects of mergers is based on the principles set out in our Mergers and Acquisitions Guidelines (our guidelines).<sup>2</sup>

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<sup>1</sup> The major grocery retailers in New Zealand are Woolworths New Zealand (Woolworths NZ), Foodstuffs North Island, and Foodstuffs South Island. The Woolworths NZ retail banners are Countdown, FreshChoice and SuperValue. The Foodstuffs North Island retail banners are PAK'nSAVE, New World and Four Square. The Foodstuffs South Island retail banners are PAK'nSAVE, New World, Four Square, Raeward Fresh and On the Spot.

<sup>2</sup> Commerce Commission, *Mergers and Acquisitions Guidelines* (May 2022).

- 7.1 We assess mergers using the substantial lessening of competition test. We determine whether a merger is likely to substantially lessen competition in a market by comparing the likely state of competition if the merger proceeds (the scenario with the merger, often referred to as the factual), with the likely state of competition if the merger does not proceed (the scenario without the merger, often referred to as the counterfactual).<sup>3</sup>
- 7.2 Only a lessening of competition that is substantial is prohibited. A lessening of competition will be substantial if it is real, of substance, or more than nominal.<sup>4</sup> There is no bright line that separates a lessening of competition that is substantial from one which is not. What is substantial is a matter of judgement and depends on the facts of each case.<sup>5</sup>
- 7.3 We must clear a merger if we are satisfied that the merger would not be likely to substantially lessen competition in any market.<sup>6</sup> If we are not satisfied – including if we are left in doubt – we must decline to clear the merger.

### **The key parties and the supply of plant-based products**

8. Life Health Foods and Chalmers are two of the largest manufacturers of plant-based food products in New Zealand.
- 8.1 Life Health Foods is based in Auckland and supplies its plant-based food products under brand names including Bean Supreme, Alternative Meat Co. and Vegie Delights.
- 8.2 Chalmers is based in Auckland and supplies its plant-based food products under the brand names Tonzu and Zenzo.
9. In New Zealand, and in other countries, there is a growing range of plant-based food products available for consumers. All industry participants advised that the demand for these types of products, particularly those which are designed to be an alternative to meat protein, is growing rapidly. Whereas in the past these products appealed largely to dedicated vegetarian and/or vegan consumers, there is a growing number of ‘flexitarian’<sup>7</sup> consumers who are looking to consume these products.<sup>8</sup>

<sup>3</sup> *Commerce Commission v Woolworths Limited* (2008) 12 TCLR 194 (CA) at [63].

<sup>4</sup> *Woolworths & Ors v Commerce Commission* (2008) 8 NZBLC 102,128 (HC) at [127].

<sup>5</sup> *Mergers and Acquisitions Guidelines* above n2 at [2.23].

<sup>6</sup> Section 66(3)(a) of the Commerce Act 1986.

<sup>7</sup> Flexitarianism is a term commonly used by those that we spoke with to describe 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>8</sup> For example, see: Commerce Commission interview with [ ]; Commerce Commission Interview with [ ]; Commerce Commission interview with [ ]; and Commerce Commission interview with [ ].

10. Table 1 below outlines the products supplied by both 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

11. As indicated in Table 1, the plant-based food products most relevant to this application are tofu, meat-alternative patties and meat-alternative sausages, as these are the products which are supplied by both of the merging parties.
- 11.1 Tofu is made by coagulating soy milk and then pressing the resulting curds into solid white blocks of varying softness.<sup>9</sup> It can then be further processed – including by flavouring, frying or baking. It is typically used as an ingredient as part of a meal.
- 11.2 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 from meat. Meat-alternative sausages can be made from a variety of ingredients.
12. 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 distributes their products to end-consumers through these customers varies. These customers include:
- 12.1 the major grocery retailers;<sup>10</sup>
- 12.2 specialty food retailers such as health food stores and specialty Asian supermarkets;

<sup>9</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.

<sup>10</sup> As above, the major grocery retailers in New Zealand are Woolworths NZ, Foodstuffs North Island and Foodstuffs South Island.

- 12.3 food service providers such as food wholesalers as well as cafés and restaurants; and
  - 12.4 home delivery food service providers.<sup>11</sup>
13. In addition to the merging parties, there are many other domestic manufacturers of plant-based food, although the range of products they each manufacture, and the customers they currently supply to, varies. These include:
- 13.1 tofu manufacturers such as Evergreen Foodstuffs Limited, which supplies tofu under its Hing's label from its factory in Wellington and Best Food Fresh Tofu Limited (Best Food), which supplies tofu under its own label from its factory in Auckland, and private label tofu manufacturers who supply tofu through the major grocery retailers; and
  - 13.2 meat-alternative manufacturers such as Food Nation Limited, which is based in Auckland, and Sustainable Foods Limited, which is based on the Kāpiti Coast.
14. As well as these domestic manufacturers, there are several other suppliers that import plant-based products into New Zealand. These include:
- 14.1 importers such as Emart Company Limited, which imports tofu under the Chongga and Bibigo labels, and ECLY Limited, which imports tofu under the Check label; and
  - 14.2 manufacturers such as Impossible Foods, which imports its own meat-alternative burger from the United States of America, and Vegetarian Delights Limited, a distributor which imports the 'Fry's' range of meat-alternative products from South Africa.

## Market definition

15. Market definition is a tool that helps identify and assess the competitive constraints the merged firm would face. Determining the relevant market(s) requires us to judge whether, for example, two products are sufficiently close substitutes as a matter of fact and commercial common sense to fall within the same market.
16. 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 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 would still impose some degree of competitive constraint on the merged entity.
17. For the reasons set out below, we have assessed the effect of the Proposed Acquisition on national markets for the wholesale supply of:

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<sup>11</sup> These sales are usually made to consumers as part of meal kits, such as My Food Bag.

- 17.1 plant-based meat-alternatives (excluding tofu) to specialty customers (such as specialty retail stores, foodservice customers and home delivery providers);
  - 17.2 plant-based meat-alternatives (excluding tofu) to major grocery retailers;
  - 17.3 tofu to specialty customers; and
  - 17.4 tofu to major grocery retailers.
18. We consider that these markets best isolate the competition that would be lost between Life Health Foods and Chalmers as a result of the Proposed Acquisition.

### **Product dimension**

19. We consider it is appropriate to define separate markets for the manufacture of tofu and for other plant-based meat-alternative products because there appears to be limited demand and supply side substitutability between these two types of products. Defining a narrow separate market for tofu also helps to isolate the key competition issues arising from the Proposed Acquisition.

### *What Life Health Foods submitted*

20. Life Health Foods considers that all types of plant-based meat-alternative products fall within the same product market.<sup>12</sup> In its view:
- 20.1 on the demand side, end consumers can and do substitute plant-based products (such as tofu, meat-alternative patties and meat-alternative sausages) with other sources of protein;<sup>13</sup> and
  - 20.2 on the supply side, the same equipment can be used to manufacture a range of different plant-based products and there are no significant barriers to switching production between types.<sup>14</sup>

### *The Commission's view*

21. We consider it is appropriate to define a market for tofu that is separate from other plant-based meat-alternative products because there appears to be limited demand and supply side substitutability between tofu and other plant-based meat-alternative products.
22. On the demand side, we received mixed evidence about how consumers (ie, shoppers and diners) buy and consume plant-based products, and how closely substitutable different products are for each other and with other sources of protein.

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<sup>12</sup> The Application at [5.32].

<sup>13</sup> Submission from Life Health Foods in response to Commerce Commission Statement of Issues at [2.1 - 2.5].

<sup>14</sup> The Application at [5.34].



For example, many market participants advised that consumer preferences for plant-based products are complex and, in some areas, fast-changing.<sup>15</sup>

23. However, most industry participants considered that consumers of tofu would not typically substitute tofu for a meat-alternative product (such as meat-alternative patties and meat-alternative sausages). This is primarily because:
- 23.1 tofu is a traditional Asian food which means there are some uses in which it will not have close substitutes.<sup>16</sup> While it may be possible to use firm tofu as a substitute for meat-alternative patties or sausages in certain situations, it may not be realistic to use softer or silken tofu, and vice-versa. For example, it is unlikely that meat-alternative sausages could be substituted for tofu in a traditional Asian meal; and
- 23.2 retailers did not consider that their customers would consider tofu and meat-alternative products to be close substitutes.<sup>17</sup> While some consumers might purchase several types of plant-based products including tofu, this, in itself, does not indicate whether these products are sufficiently close substitutes that consumers would switch between if the relative price of one of the products increased.
24. On the supply side, the manufacturing process to make tofu is quite different to making meat-alternative patties and meat-alternative sausages. Most manufacturers cannot easily switch production between tofu and meat-alternative patties and sausages. However, the evidence suggests that suppliers can more readily switch production between other plant-based meat-alternative products.
- 24.1 Meat-alternative patties and sausages can be made using a variety of ingredients<sup>18</sup> and are manufactured using similar equipment. The main difference in the products is its final shape.<sup>19</sup>
- 24.2 Conversely, tofu is made using soybeans as the main input, which then undergoes a process of coagulation.<sup>20</sup> To this extent, manufacturers of tofu would require significant investment in new equipment to switch to making other products such as meat-alternative patties and sausages.<sup>21</sup>

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

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

<sup>17</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ]; Commerce Commission interview with [ ]. [ ] data from [ ] in response to Commerce Commission request for information.

<sup>18</sup> These ingredients are typically texturized vegetable proteins from a variety of sources such as soybeans and hempseed.

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

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

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

25. Further, all industry participants, other than the merging parties, noted that Life Health Foods and Chalmers are the two largest domestic manufacturers of tofu. Defining a narrow market for the supply of tofu that is separate from other meat-alternative products is therefore likely to best isolate the competition issues that arise from the Proposed Acquisition.

### **Customer dimension**

26. Major grocery retailers are the main customers of suppliers of tofu and meat-alternative products and their supply alternatives appear to be different to other specialty customers.<sup>22</sup> This means that the competitive effects of the Proposed Acquisition may be different for the major grocery retailers than for other specialty customers. As such, for each product market, we consider it appropriate to define separate customer markets for supply to the major grocery retailers and to specialty customers.

#### *What Life Health Foods submitted*

27. Life Health Foods acknowledged that there are some differences in the requirements between the main customers in relation to tofu and meat-alternative products but submitted that these differences are not sufficiently material to define separate customer markets.<sup>23</sup> In its view:
- 27.1 producers supply their plant-based products to all customers in the same product size and in the same packaging, regardless of whether the retail customer is a specialty food store, a hospitality outlet or a supermarket; and
- 27.2 producers often deliver their plant-based products direct to store and there are no significant differences in the volume, and frequency, of their deliveries to a specialty store, such as an Asian supermarket, compared to a supermarket operated by one of the major grocery retailers.<sup>24</sup>

#### *The Commission's view*

28. We consider that, for each relevant product type, it is appropriate to define separate customer markets for supply to the major grocery retailers and for the supply to all other customers.
29. While there is little differentiation between the tofu products (and meat-alternative products in general) that suppliers supply to each different type of wholesale customers,<sup>25</sup> the requirements to supply speciality retailers, such as Asian

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Commission interview with [ ].

<sup>22</sup> As noted above, these specialty customers include: specialty food retailers such as health food stores and specialty Asian supermarkets; food service providers such as food wholesalers as well as cafés and restaurants; and home delivery service providers.

<sup>23</sup> The Application at [5.42].

<sup>24</sup> The Application at [5.44].

<sup>25</sup> For example, the same product types, in similar pack sizes, are supplied by the merging parties to major grocery retailers and all other customers including Asian supermarkets. Commerce Commission interview

supermarkets or other foodservice customers, appear to be different than for the major grocery retailers.<sup>26</sup> In particular, in contrast to supplying speciality retailers, supplying tofu and other meat-alternative products to the major grocery retailers requires:

- 29.1 a greater range of product lines (such as different flavours and styles); and
  - 29.2 more regular deliveries of each product and in greater volumes.<sup>27</sup>
30. Further, several smaller suppliers stressed that supplying the major grocery retailers required them to be actively involved in promotional and marketing activities, which is not typically required by many of the speciality retailers.<sup>28</sup> This activity, together with the volume and ranging requirements of the major grocery retailers, meant that it is significantly more difficult to supply the major grocery retailers than speciality retailers. This appears to be particularly relevant in the supply of tofu, where:
- 30.1 there are currently significantly more suppliers of tofu to speciality retailers than there are to the major grocery retailers; and
  - 30.2 the merging parties are the two most prominent suppliers to the major grocery retailers.
31. Accordingly, it appears that, for each relevant product, the major grocery retailers may have fewer existing options for suppliers than other customers, which may enable the merged entity to price discriminate between different customer groups. Speciality retailers on the other hand appear to have a greater range of supply options available to them, due to their lower volume, logistics and ranging requirements.
32. Therefore, we consider that, in order to best isolate any potential competition concerns arising from the Proposed Acquisition, it is appropriate to define separate customer markets for the supply of tofu (and separately meat-alternative products) to the major grocery retailers and for supply to all other customers.

### Other market dimensions

33. The merging parties both supply the major grocery retailers as well as the other speciality retail, foodservice customers and home delivery providers, and so the appropriate functional level is the wholesale level.<sup>29</sup>

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with [ ]; Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>26</sup> For example, see Commerce Commission interview with [ ]; Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>27</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

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

<sup>29</sup> The Application at [5.40]; Commerce Commission interview with Life Health Foods [ ].

34. While we received feedback that consumer tastes and preferences for tofu and meat-alternative products may vary by location or region,<sup>30</sup> such differences do not appear to be sufficient to define separate geographic markets. All the major suppliers of tofu and meat-alternatives supply their products nationally either directly or via third party distributors.<sup>31</sup> Accordingly, for each relevant market, we consider the markets are national in scope.

#### **Conclusion on approach to market definition**

35. We consider the most appropriate way to assess the effect of the Proposed Acquisition on competition is to define national markets for the wholesale supply of:
- 35.1 plant-based meat-alternatives (excluding tofu) to specialty customers;
  - 35.2 plant-based meat-alternatives (excluding tofu) to major grocery retailers;
  - 35.3 tofu to specialty customers; and
  - 35.4 tofu to major grocery retailers.
36. We consider that these relevant markets are likely to best isolate the competitive constraint that Life Health Foods and Chalmers exert on each other, which would be lost with the Proposed Acquisition.

#### **With and without scenarios**

37. Assessing whether a substantial lessening of competition is likely requires us to:
- 37.1 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
  - 37.2 to determine whether competition is likely to be substantially lessened by comparing those scenarios.
38. With the acquisition, Life Health Foods would acquire the business and assets of Chalmers.
39. Without the acquisition, the status quo is likely to continue and so Chalmers would continue to operate independently and compete with Life Health Foods.<sup>32</sup>

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<sup>30</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>31</sup> The Application at [5.37]. Commerce Commission interview with Life Health Foods [ ]; Commerce Commission interview with [ ].

<sup>32</sup> The Application at [3.8]; Commerce Commission interview with Chalmers [ ].

## How the Proposed Acquisition could substantially lessen competition

40. Our investigation focused on whether the Proposed Acquisition would be likely to substantially lessen competition by assessing the potential for unilateral, coordinated and conglomerate effects.
41. Unilateral effects can arise when a firm merges with, or acquires, a competitor that would otherwise provide a significant competitive constraint. The Proposed Acquisition could substantially lessen competition due to unilateral effects if, in any relevant market, the competition lost between the merging parties' products allowed the merged entity to profitably increase the wholesale price and/or reduce the quality of its products.
42. Coordinated effects can occur when a merger or acquisition makes it significantly more likely that the remaining firms in a market can collectively exercise market power to increase prices, restrict output or reduce quality.
43. Conglomerate effects can occur when a merged firm gains the ability or incentive to foreclose competitors by using anticompetitive strategies that leverage its market power in a market into another market where it otherwise faces more competition. In this matter we have focussed particularly on whether the Proposed Acquisition changes the ability or incentive of the merged entity to engage in anticompetitive tying or bundling strategies.

## Competition assessment – the meat-alternative markets

44. In the two relevant meat-alternative markets, we consider the Proposed Acquisition will not have, or would not be likely to have, the effect of substantially lessening competition due to unilateral effects or coordinated effects. We set out our reasoning for these assessments below.

### Unilateral effects in the market for the supply of meat-alternatives to speciality customers

45. Regardless of how the market is defined, Life Health Foods submitted that the Proposed Acquisition would not be likely to substantially lessen competition for the supply of any meat-alternative product because the merged entity will continue to face vigorous, and growing, competition from a large number of alternative suppliers, who face low barriers to entry and expansion.<sup>33</sup>
46. There is growing demand in the food service and hospitality industries for meat-alternative products and there are several domestic and overseas based suppliers including Vegetarian Delights Limited, Impossible Foods and Goodman Fielder New Zealand Limited. We understand that none of these suppliers face significant barriers to expansion.<sup>34</sup> Further, neither Life Health Foods nor Chalmers supply any significant volumes of their meat-alternative products to any speciality customers as

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<sup>33</sup> The Application at [6.1].

<sup>34</sup> For example, Commerce Commission interview with [ ]; Commerce Commission interview with [ ]; Commerce Commission interview with [ ]

they have both concentrated on supplying their products to the major grocery retailers.

47. To this extent, given the limited overlap between the merging parties and the presence of existing competitors, we are satisfied that the Proposed Acquisition will not have, and would not be likely to have, the effect of substantially lessening competition in the supply of meat-alternatives to speciality customers market due to unilateral effects.

**Coordinated effects in the market for the supply of meat-alternatives to speciality customers**

48. Neither of the merging parties are significant suppliers into this market, and the merged entity would compete with several other suppliers of varying size, scale and cost bases. As such, the merger would be unlikely to change any of the conditions that would make coordination more likely, complete, or sustainable.
49. Accordingly, we consider it unlikely that the Proposed Acquisition would result in a substantial lessening of competition in the supply of meat-alternatives to specialty customers by way of coordinated effects.

**Unilateral effects in the market for the supply of meat-alternatives to the major grocery retailers**

50. Both Life Health Foods and Chalmers supply a range of meat-alternative products to the major grocery retailers. Several industry participants noted that the merging parties' ranges of meat-alternative burger patties and sausages have grown over time and now both ranges have prominent positions in a typical supermarket.<sup>35</sup> Market share estimates provided by the Applicant indicated that the merging parties would account for the majority of the meat-alternative products sold in the stores of the major grocery retailers.<sup>36</sup>
51. However, all industry participants advised the tastes and preferences of consumers in this market are rapidly changing. Whereas meat-alternative products used to only target vegetarian and vegan consumers, we understand that these products are becoming more and more popular with consumers who are looking to reduce their meat consumption.<sup>37</sup>
52. With this in mind, we consider that current market shares are likely not an accurate representation of competitive dynamics in this market and instead likely represent the merging parties being the first to market with these products.<sup>38</sup> Indeed, the major grocery retailers commented that they have not encountered any difficulties

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

<sup>36</sup> The Application at Table 7 and Table 8.

<sup>37</sup> For example, see Commerce Commission interview with [ ]; Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>38</sup> Commerce Commission interview with [ ].

in acquiring supply of meat-alternative products from a range of other manufacturers.

53. The increasing demand for meat-alternative products encourages product innovation from a range of different manufacturers and there has been recent entry and expansion from a variety of different suppliers in direct competition with the meat-alternative products of the merging parties. None of these suppliers indicated there are significant barriers to them increasing the quantity of meat-alternative products they currently manufacture.<sup>39</sup> These suppliers include:
- 53.1 domestic manufacturers such as Sustainable Foods Limited and Food Nation Limited as well as Sunfed Limited;<sup>40</sup> and
- 53.2 international companies who supply imported meat-alternatives products such as Impossible Foods and Vegetarian Delights Limited as well as Linda McCartney Foods.<sup>41</sup>
54. To this extent, given the presence of existing competitors with an ability to expand, and the clear ability of major grocery retailers to switch away from the merged entity, we are satisfied that the Proposed Acquisition will not have, and would not be likely to have, the effect of substantially lessening competition in the supply of meat-alternatives to the major grocery retailers market due to unilateral effects.

#### **Coordinated effects in the market for the supply of meat-alternative products to the major grocery retailers**

55. The merged entity would be one of the largest suppliers of meat-alternative products to the major grocery retailers. As noted above, there are several other existing suppliers and industry participants of varying scale, and the major grocery retailers are able to promote competition from these sources. In addition, there is limited market transparency as wholesale prices are confidential and negotiated privately and bilaterally. These features are likely to make it difficult to reach and monitor coordination.
56. Market conditions may also make any coordination unstable. In particular, consumer demand is increasing and preferences regarding plant-based meat-alternatives are rapidly evolving. Entry and expansion by other suppliers in response to these dynamics does not seem difficult as the major grocery retailers would have incentives to support entry and expansion of other suppliers as demand evolves.<sup>42</sup>
57. Accordingly, we are satisfied that the Proposed Acquisition will not have, and would not be likely to have, the effect of substantially lessening competition in the market

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<sup>39</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>40</sup> Sunfed Limited is a New Zealand-based supplier of plant-based chicken, beef, and bacon.

<sup>41</sup> Linda McCartney Foods is a British food brand that specialises in vegetarian and vegan foods.

<sup>42</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

for the supply of meat-alternatives to the major grocery retailers by way of coordinated effects.

### **Competition assessment – the tofu markets**

58. In the two relevant tofu markets, we consider the Proposed Acquisition will not have, or would not be likely to have, the effect of substantially lessening competition due to unilateral effects or coordinated effects. We set out our reasoning for these assessments below.

#### **The Applicant's submissions on competitive effects in the supply of tofu**

59. Regardless of how the markets are defined, Life Health Foods submitted that the Proposed Acquisition would not be likely to substantially lessen competition for the supply of tofu primarily because:
- 59.1 Life Health Foods and Chalmers are not each other's closest competitor in the supply of tofu. Rather, the merging parties current face vigorous competition from a range of existing suppliers and there are limited barriers to these suppliers expanding;<sup>43</sup> and
- 59.2 as the main customers, the major grocery retailers would have significant countervailing power over the merged entity.<sup>44</sup>

#### **Unilateral effects in the market for the supply of tofu to speciality customers**

60. Post-acquisition, the merged entity is likely to be constrained in the supply of tofu to specialty customers by a range of existing competitors and there are limited constraints on these suppliers expanding the supply of tofu to those customers.<sup>45</sup>
61. Life Health Foods and Chalmers only supply limited volumes of their tofu to specialty customers and no industry participants considered they are close competitors for those customers. While Life Health Foods and Chalmers have increased the amount of tofu they produce significantly in recent years, almost all their tofu is supplied to the major grocery retailers rather than to speciality retailers.<sup>46</sup>
62. Industry participants advised that Asian supermarkets and other speciality retailers have historically always stocked tofu and there is an established base of

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<sup>43</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [5.1] and [5.3].

<sup>44</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [1.2 (d)].

<sup>45</sup> For example, see Commerce Commission interview with [ ]; Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>46</sup> For example, both Life Health Foods and Chalmers advised that they have only recent started supplying tofu to Asian supermarkets. At present, specialty customers account for approximately [ ] of the tofu that Life Health Foods supplies, with most of this supply going to foodservice/hospitality customers. Specialty customers account for approximately [ ] of the tofu that Chalmers supplies, with most of this supply going to home delivery customers. See The Application and Commerce Commission interview with Chalmers [ ].



manufacturers, other than the merging parties, who supply them with tofu. These include:

- 62.1 domestic manufacturers based in Auckland, such as Soy Works Company Limited, Best Food, ECLY Limited as well as Capital Canton Tofu Company Limited and Green Mount Tofu;
  - 62.2 domestic manufacturers based in Wellington, such as Evergreen Foodstuffs Limited (with its Hing's branded tofu) as well as Phoenix Tofu; and
  - 62.3 importers of tofu produced overseas, such as Emart Company Limited.
63. To this extent, given the limited overlap between the merging parties and the presence of existing competitors, we are satisfied that the Proposed Acquisition will not have, and would not be likely to have, the effect of substantially lessening competition in the market for the supply of tofu to speciality customers due to unilateral effects.

#### **Coordinated effects in the market for the supply of tofu to speciality customers**

64. We are satisfied that the Proposed Acquisition will not have, and would not be likely to have, the effect of substantially lessening competition in the market for the supply of tofu to specialty customers by way of coordinated effects. In particular, we note that the merged firm will have only a small presence in this market and will compete with a number of other suppliers of varying sizes. The Proposed Acquisition will not change any other conditions in this market such that coordination would be more likely, complete or sustainable.

#### **Unilateral effects in the market for the supply of tofu to the major grocery retailers**

65. The merging parties are each other's closest competitors in supplying tofu to the major grocery retailers. Further, the merged entity would supply a significant proportion of the tofu sold via the major grocery retailers and, absent any intervention by the major grocery retailers, would not be significantly constrained by other existing competitors under current conditions.
66. However, each of the major grocery retailers is likely to have significant buyer power in its dealings with the merged entity in this market. In addition, we consider that by facilitating expansion of smaller suppliers and/or expanding sales of private label products, the major grocery retailers would be able to credibly threaten to bypass the merged entity if it sought to exercise unilateral market power. This countervailing buyer power is likely to constrain the merged entity in the supply of tofu to the major grocery retailers.
67. Accordingly, we are satisfied that the Proposed Acquisition will not have, and would not be likely to have, the effect of substantially lessening competition in the market for supply of tofu to the major grocery retailers due to unilateral effects.

*Life Health Foods and Chalmers are each other's closest competitor in supplying tofu to the major grocery retailers*

68. Our inquiries indicate that Life Health Foods and Chalmers are each other's closest competitor in the supply of tofu to the major grocery retailers and this competition would be lost as a result of the Proposed Acquisition.
69. Life Health Foods considers that the merging parties are just two suppliers of tofu that compete closely with all other plant-based product manufacturers.<sup>47</sup> However, all industry participants considered that Life Health Foods and Chalmers are the two most prominent suppliers of tofu to the major grocery retailers, as indicated by the shelf space allocated to their tofu products in the supermarkets of Woolworths NZ and the two Foodstuffs entities. This shelf space is reflected in the market share estimates that are included in the Attachment. In particular, we understand that:
- 69.1 the merging parties' tofu brands have significant brand recognition and loyalty in the supermarkets of the major grocery retailers;<sup>48</sup> and
- 69.2 the merging parties supply similar tofu ranges and in many supermarkets, particularly the smaller stores and/or those outside of the main centres, they tend to be the only suppliers of tofu that are typically stocked in the supermarket.<sup>49</sup>

*Constraint from existing competition in supplying tofu to the major grocery retailers*

70. At present, Life Health Foods and Chalmers supply a significant share of the tofu sold in the major grocery retailers' supermarkets. While there are several other tofu suppliers that would compete with the merged entity for supply to the major grocery retailers, we consider the constraint provided by these existing suppliers by itself would not be likely to sufficiently constrain the merged entity in the supply of tofu to the major grocery retailers.
71. All industry participants noted that, in addition to Life Health Foods and Chalmers, there are several other suppliers of tofu to the major grocery retailers although the presence of these suppliers in individual supermarkets can vary significantly, as indicated by the market share estimations in the Attachment. These suppliers include:
- 71.1 Evergreen Foodstuffs Limited (with its Hing's tofu);

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<sup>47</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [2.3]-[2.4].

<sup>48</sup> For example, we received feedback that [ ], if one brand's tofu product is not available, customers will look to switch to another tofu product of the same brand, before switching to a comparable product from a different brand. See Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>49</sup> Commission assessment of data from the major grocery retailers. For example, other suppliers' tofu products are only stocked in between [ ]% of the supermarkets of the major grocery retailers. Also see Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

- 71.2 Best Food;
- 71.3 The Soy Works Company Limited; and
- 71.4 Emart Company Limited (with Chongga and Bibigo branded tofu).
72. All these existing suppliers also have a presence in the market for the supply of tofu to speciality customers and all supply tofu that is of equivalent quality as the merging parties'. However, the total volume of tofu that each of these manufacturers currently produce is significantly less than that which Life Health Foods and Chalmers currently supply to the major grocery retailers. This is primarily because these manufacturers have typically focused on supplying tofu to speciality customers rather than to the major grocery retailers.
73. To provide a constraint on the merged entity in this market, we consider that existing suppliers would need to actually increase their supply of tofu to the major grocery retailers, or otherwise be able to do so in a relatively short timeframe. Several manufacturers advised that they do not have the existing infrastructure to do this.<sup>50</sup> Rather, they would require investment to:
- 73.1 increase their overall production capabilities;
- 73.2 expand their overall range of tofu products; and
- 73.3 expand their distribution capabilities.
74. We do not consider such investment to be insurmountable for an existing supplier.<sup>51</sup> However, before any investment is undertaken by an existing tofu manufacturer, the manufacturer would need to be sufficiently confident that there will be enough demand for its tofu to make the investment worthwhile. In our view, any investment would likely be linked to a supply relationship with a major grocery retailer. We discuss this further below in relation to countervailing power.

*Countervailing power of the major grocery retailers*

75. A merged firm's ability to increase prices profitably may be constrained by the ability of certain customers to exert substantial influence on negotiations. Countervailing power exists when a customer possesses special characteristics which give that customer the ability to substantially influence the price that the merged firm charges.
76. The merging parties are currently the main suppliers of tofu to the major grocery retailers and, as noted above, other suppliers are currently constrained in their ability to expand their sales in this market. However, we consider that if incentivised

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<sup>50</sup> For example, see Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>51</sup> For example, [ ].

to do so, the major grocery retailers could switch to alternative suppliers, either by promoting entry by new suppliers, expansion of existing smaller suppliers, or increasing supply of private label products. As the merged entity would rely on the major grocery retailers for the majority of its tofu sales, we consider that the major grocery retailers' countervailing power is likely to be sufficient to constrain the merged entity from exercising unilateral market power.

77. The extent of the major grocery retailers' countervailing buyer power will depend on the relative strength of their bargaining power in dealing with the merger parties. This, in turn, will depend on the relative value of the 'outside options' that are available to each party if they walk away from bilateral negotiations.
78. In this market, or even if we were to consider a wider market for supply of all tofu, the major grocery retailers make up a significant proportion of the tofu purchases and a significant proportion of the revenues of the merging parties. We therefore consider that the balance of bargaining power is likely to lie with the major grocery retailers in both the factual and counterfactual even though the merged entity would account for a large share of the current supply of tofu to each of these retailers. This is because the merged entity is likely to have relatively weaker 'outside' supply options in the event of a major grocery retailer ceasing to purchase its tofu.
79. We hold this view because if one of the major grocery retailers significantly reduced its tofu purchases from the merged entity, that entity would struggle to divert these volumes to other customers, and to other markets, for the following reasons:
- 79.1 the loss is unlikely to be absorbed by category sales growth;
- 79.2 speciality customers purchase low volumes of tofu compared to the major grocery retailers,<sup>52</sup> and they are currently well supplied and in some cases, have close relationships with their suppliers,<sup>53</sup> and
- 79.3 nearby export markets are well-served and highly competitive. For example, in Australia there are numerous large tofu suppliers with significant excess capacity.<sup>54</sup>
80. By contrast, we consider it likely that the major grocery retailers would have relatively strong options for replacing any reduction in tofu volumes purchased from the merged entity if the merged entity attempted to exercise unilateral market power. It is likely that the major grocery retailers would look to replace volumes

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<sup>52</sup> For example, between [ ] of the tofu supplied by each of the merging parties is purchased from a supermarket operated by one of the major grocery retailers. Commerce Commission interview with [ ]; Commerce Commission interview with [ ]; Email from [ ] to Commerce Commission [ ].

<sup>53</sup> Commerce Commission interview with [ ]. Commerce Commission interview with [ ].

<sup>54</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

from the merged entity with purchases from other tofu suppliers, rather than reduce the overall volumes of tofu they offer consumers in their stores.

81. As discussed above, we understand that existing smaller tofu suppliers currently face barriers to expanding to supply the major grocery retailers. However, we also understand that the major grocery retailers would be able to take steps to encourage the expansion of existing manufacturers, if sufficiently incentivised by the actions of the merged entity to do so. For example:

81.1 Foodstuffs North Island advised that if faced with an unjustified price increase from the merged entity,  
[

].<sup>55</sup>

81.2 Woolworths NZ said that if the merged entity tried to increase its prices beyond what is considered reasonable,  
[ ]. It also provided the example of [ ],<sup>56</sup> with whom it could leverage its pre-existing relationship to begin supplying branded products alongside Macro-branded tofu.

82. As a result, we consider that the major grocery retailers would have countervailing power in their dealings with the merged entity because they would have other options to turn to if the merged entity attempted to exercise unilateral market power, be it alternative suppliers or self-supply. The major grocery retailers would likely be able to use this countervailing power to constrain the merged entity. This imbalance would be common knowledge to the retailer and the merged entity in any negotiation over wholesale prices.<sup>57</sup>

### **Coordinated effects in the market for the supply of tofu to the major grocery retailers**

83. Similar to the supply of meat-alternative products, the merged entity would be one of the largest suppliers of tofu to the major grocery retailers, which would mean that its incentives to coordinate with other suppliers post-acquisition will be weak. As noted above, the major grocery retailers are large, sophisticated customers who would likely notice the effect of any coordination and have several other options from which to increase the volumes they acquire supply from in the case of coordination.<sup>58</sup>

84. Accordingly, we satisfied that the Proposed Acquisition will not have, and would not be likely to have, the effect of substantially lessening competition market for the supply of tofu to the major grocery retailers by way of coordinated effects.

<sup>55</sup> Commerce Commission interview with [ ].

<sup>56</sup> [ ] manufactures Woolworths' Macro tofu.

<sup>57</sup> Commerce Commission interview with [ ].

<sup>58</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

## Conglomerate effects

85. Conglomerate effects arise when the merged entity would gain market power in a market or markets and would be likely to leverage that into any of the other, more competitive markets. The merged entity may be able to do so by linking the sales of multiple goods, for example by tying, bundling or technical integration. While linking sales in these ways may promote competition, it can undermine it when a firm has market power over some goods and structures its offers to prevent efficient rivals in more competitive markets from gaining customers.
86. However, we saw no evidence that the Proposed Acquisition would result in a substantial lessening of competition by way of conglomerate effects.
- 86.1 At present, the merging parties have similar product ranges and so Life Health Foods would not be acquiring any new or ‘must have’ products. The only product of Chalmers that Life Health Foods doesn’t currently make is tempeh and tempeh only accounts for a small proportion of Chalmers’ existing sales.
- 86.2 Life Health Foods is affiliated with the Sanitarium Health and Wellbeing Company, which supplies a wide range of food products supplied through the major grocery retailers. This is an existing situation and we saw no evidence that the Proposed Acquisition would give the merged entity the ability or incentives to offer tied or bundled deals that would likely prevent other suppliers of individual products from competing with the merged entity and/or with the Sanitarium Health and Wellbeing Company.<sup>59</sup>
87. Accordingly, we are satisfied that the Proposed Acquisition will not have, and would not be likely to have, the effect of substantially lessening competition in any market by way of conglomerate effects.

## Overall conclusion

88. For the reasons outlined above, we are satisfied that the Proposed Acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in any of the relevant markets.

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<sup>59</sup> For example, [

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**Determination on notice of clearance**

89. Under section 66(3)(a) of the Commerce Act 1986, the Commerce Commission determines to give clearance Life Health Foods NZ Limited to acquire the business and assets of Chalmers Organics Limited.

Dated this 26<sup>th</sup> day of May 2022

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Anna Rawlings  
Chair

**Attachment: market share estimates**

**Table A: Commission estimates of the market shares in the supply of tofu to the major grocery retailers**

Supplier	Brand	2019		2020		2021	
		Sales	Share	Sales	Share	Sales	Share
Life Health Foods	Bean Supreme	[ ]					
Chalmers	Tonzu						
<i>Merged entity</i>							
Woolworths Private Label [ ]	Macro						
Evergreen Foodstuffs Limited	Hing's						
Morinaga	Mori-Nu						
Best Food	Best Food Fresh						
The Soy Works Company Limited	Soy Works, Tofuman						
Emart Company Limited	Chongga, Bibigo						
ECLY Limited	Check						
Other							]
<b>Total sales</b>		<b>[ ]</b>	<b>100%</b>	<b>[ ]</b>	<b>100%</b>	<b>[ ]</b>	<b>100%</b>
<b>Major grocery retailer split of total sales</b>		Foodstuffs	[ ]	Foodstuffs	[ ]	Foodstuffs	[ ]
		Woolworths	[ ]	Woolworths	[ ]	Woolworths	[ ]

Source: Foodstuffs North Island, Foodstuffs South Island, Woolworths NZ. Includes rounding errors.