

PUBLIC VERSION

4 April 2022

LIFE HEALTH FOODS/ CHALMERS ORGANICS

SUBMISSION OF LIFE HEALTH FOODS NZ LIMITED ON STATEMENT OF ISSUES

1. INTRODUCTION AND EXECUTIVE SUMMARY

1.1 This submission is made by Life Health Foods NZ Limited (**LHF**) in response to the Commerce Commission's (**Commission**) Statement of Issues (**SOI**) dated 23 March 2022.

1.2 For the reasons set out below:

- (a) tofu is substitutable for a wide range of plant-based meat alternatives and meat products;
- (b) tofu is a product within a broader national market for the wholesale supply of meat alternatives products to the national supermarket chains, Asian supermarkets, speciality food stores and local food retailers. Asian supermarkets in particular are recognised by the two national supermarket chains as close competitors in their specialist category;
- (c) barriers to entry and expansion are very low. It is not difficult for existing suppliers to increase the quantity and range of their tofu products or for new suppliers to enter the market; and
- (d) the two nationwide supermarket chains have significant countervailing power. They are able through their ranging decisions and shelf space allocations to provide preferential positioning for their own private label products and encourage entry and expansion of new and smaller players.

2. THE SUBSTITUTABILITY BETWEEN DIFFERENT TYPES OF PLANT-BASED PRODUCTS, IN PARTICULAR IN RELATION TO WHICH PRODUCT(S) CAN BE USED AS SUBSTITUTES FOR TOFU

2.1 As previously submitted, there are a very limited number of exclusive tofu shoppers in New Zealand – the population representative research from Nature Research found [redacted]% of respondents purchased only tofu, as shown in the analysis below. There are high levels of cross shopping occurring with other plant-based protein segments and animal protein sources.

[redacted]

2.2 Tofu and plant-based meat alternatives are stocked in the same shelf location at major supermarkets and other retail outlets, and all compete for available shelf space. The price of each product is displayed on price ticketing immediately below each product enabling shoppers to easily compare prices. The photos below show typical store layouts with tofu displayed alongside a wide range of plant-based products:



Countdown Ponsonby, 23 March 2022



Pak'n Save Kilbirnie, July 2021

- 2.3 While there is no data available to answer the hypothetical question 'what will consumers do' in response to a price increase, with many alternative plant-based and animal protein options available LHF would expect an increased level of switching to these alternative segments if the price of tofu became too high.
- 2.4 Because there are many more 'flexitarian' consumers than exclusively vegetarian or vegan customers, the major constraint to sales of plant-based foods (including tofu) is the price relativity to animal protein, which typically sells, per kilo, at lower prices than plant-based equivalents. A price increase for tofu is likely to lead consumers to switch to other plant-based products or meat products.
- 2.5 Tofu is used in a variety of different meal occasions, resulting in a differing range of alternatives that could be used as a substitute for tofu, as illustrated in Table 1 below:

Table 1: Tofu Substitutes

Typical Use for Tofu	Potential Substitutes
Stir Fry	Plant-based chicken strips / chunks, sausages Chicken / Beef Strips / Seafood
Curry	Plant-based chicken strips / chunks, sausages, falafel, paneer Chicken / Beef / Lamb / Seafood Pulses and Legumes such as Dahl / Chickpea Vegetables such as Eggplant
Steak / Burger	Plant-Based Burger Patties (made from ingredients such as beetroot, cauliflower, legumes and grains) Mushrooms Beef / Lamb / Pork / Chicken / Seafood
Crumbled or Grated, Mince Style	Plant-Based Mince, Dried TVP (Textured Vegetable Protein), Legumes / Lentils / Rice Jackfruit Falafel Beef / Lamb / Pork / Chicken Mince
Crumbed / Fried	Plant-based nuggets, schnitzels, crumbed burgers Haloumi, Banana Flowers, Eggplant, Mushrooms Chicken / Beef / Veal / Seafood

3. THE RELEVANT MARKET(S), IN PARTICULAR IN RELATION TO THE SUPPLY OF TOFU

3.1 As set out in [5.30] of LHF’s Notice seeking clearance dated 17 December 2021 (**Notice**) LHF does not agree that there is a discrete market for the wholesale supply of tofu and considers tofu to be part of a broader meat alternatives product market. In this submission we respond to the Commission’s questions in relation to the tofu segment of that broader market.

Geographic scope

3.2 As set out in [5.37] – [5.39] of the Notice, LHF maintains that the geographic scope of the market is nationwide. While some retailers, in particular Foodstuffs North Island and South Island, allow for small players to supply locally to individual stores, they still undertake range reviews for core range in New World and Pak’n Save stores which are expected to be stocked by all stores.

3.3 It is typical in New Zealand for small players and new entrants to start on a regional basis and expand over time with wider distribution and ranging. This “start small and expand” approach is in fact how Bean Supreme and Chalmers entered the market and is seen with more recent category entrants such as Sunfed Plant-based Chicken. There are numerous other similar examples in other categories; for instance, Pics Peanut Butter is a well-publicised example of building up to national ranging after small beginnings.

Product Dimension

- 3.4 As explained at [5.30] – [5.35] of the Notice, LHF’s view is that the product dimension of the market is plant-based products (including tofu).

Customer Dimension

- 3.5 As set out at [5.30] – [5.35] of the Notice, LHF considers the customer dimension of the market to comprise the national supermarket chains, Asian supermarkets, speciality food stores and local food retailers.
- 3.6 LHF submits that the Commission’s preliminary view that the wholesale supply of tofu to “*major grocery retailers*” is a separate market is inconsistent with the facts and contrary to commercial common sense.
- 3.7 The Commission separates supply to the two national supermarket chains from supply to Asian supermarkets on the basis that “the major grocery retailers typically place more stringent requirements on suppliers, and demand an expanded range of products (eg, different pack sizes, flavours) that other customer types do”.¹ While this may be the case for western products, the situation is reversed for Asian products. Tofu is a traditional component of East Asian and Southeast Asian cuisines, so it should not come as a surprise that Asian supermarkets stock a greater range of, and typically sell more, tofu than equivalent sized western supermarkets.
- 3.8 Submissions to the Commission’s retail grocery market inquiry recognised that Asian supermarkets competed with traditional supermarkets in this category:
- (a) Woolworths NZ identified Asian supermarket chain Tai Ping as a retail chain that competed with it very effectively;²
 - (b) Foodstuffs NI noted that the ACCC had concluded that speciality stores such as Asian supermarkets “*tend to compete with the major retailers on quality and service offering*”,³ and
 - (c) Foodstuffs NI submitted that “*the nature and closeness of competition (and thus a degree of constraint) depends on related factors such as the nature of the smaller grocery retailer. For example, a specialist retailer such as a pet food retailer constrains the retailer in the particular category*”.⁴
- 3.9 The reality is that the “*major grocery retailers*” stock a smaller range of tofu than Asian supermarkets, and many specialist retailers. Asian supermarkets are the leaders in the tofu category. It is the western supermarket chains which are the followers. The Commission’s preliminary view that the Western supermarkets demand a more expanded range of tofu, or place more stringent requirements on tofu suppliers, than Asian supermarkets, is simply wrong.
- 3.10 LHF notes many new entrants initially supply Asian Supermarkets or specialty retail channels, then in time selected Foodstuffs stores before growing to nationwide supermarket representation. This is in fact consistent with Bean Supreme and Chalmers history (both began in speciality retail channels) and is also the case for Hings and Check tofu brands.
- 3.11 LHF also notes that in the plant-based food category, the same physical product formats are typically sold by suppliers into grocery, food service, and home delivery providers. For example, LHF sells the same (identical) Firm Tofu 300g pack to grocery, wholesalers and home delivery customers including Foodstuffs, Woolworths NZ, Bidfood, Gilmours and Hello Fresh.
- 3.12 LHF also challenges the Commission’s preliminary view⁵ that major grocery retailers require suppliers to provide an expanded range of product. By way of example, in the Plant-Based foods category,

² Woolworths NZ *Submission on retail grocery market study preliminary issues paper* 4 February 2021

³ Foodstuffs NI *Post conference submission on market study into grocery sector* 3 December 2021

⁴ Foodstuffs NI *Submission on retail grocery market study preliminary issues paper* 4 February 2021

⁵ SOI at [38]

Sunfed, initially supplied a single plant-based chicken style product, growing to in excess of \$1m of sales with that solitary product.

4. HOW CLOSELY LHF AND CHALMERS COMPETE TO SUPPLY TOFU TO THE MAJOR GROCERY RETAILERS

- 4.1 Within the tofu segment, Firm Tofu block format is common to all major suppliers, including LHF and Chalmers. In Marinated Tofu, LHF supplies in block form, whereas Chalmers offers a cube form. Neither supplier offers soft or silken formats and only Chalmers supplies Tempeh which is considered part of the tofu segment.
- 4.2 LHF notes that other brands also supply more than one size/variety of Tofu. Private Label competes strongly in the Tofu segment with LHF and Chalmers products, particularly in Woolworths where the Macro offer is well established.
- 4.3 Other brands such as Hings and Check, whilst currently ranged in fewer stores, compete vigorously with multiple product formats, and in fact outsell LHF and Chalmers tofu products where stocked.
- 4.4 Table 2 below summarises the various product formats supplied by selected suppliers:

Table 2: Tofu Product Format

Product format	LHF	Chalmers	Hings	Check	Macro
Firm Tofu Block	✓	✓	✓	✓	✓
Marinated Tofu Block	✓				✓
Marinated Tofu Cubes		✓			
Soft / Silken Tofu			✓	✓	
Tempeh		✓			

- 4.5 The Commission’s preliminary view⁶ that ‘in many parts of the country the merging parties’ products are the only brands stocked’ is incorrect. Macro tofu is sold in []% of Woolworths NZ stores; whilst recently launched Pams tofu is stocked in []% of all New World and Pak’n Save stores nationally and is expected to climb further over the coming months consistent with other Pams product ranging. Other brands such as Hings, Check, and Mori-Nu products are stocked in []% of stores.

5. 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

5.1 It is not difficult for existing suppliers to increase the quantity and range of their tofu products. Chalmers is a good example. []

5.2 []

5.3 Both Hings and Check, prominent suppliers of tofu to Asian Supermarkets and specialist retailers are well placed to follow a similar path to Chalmers if they wish to do so, including scaling up supply of tofu more broadly into western supermarkets nationwide. Hings and Check tofu is already sold to selected Pak’n Save North Island and New World North Island stores and as previously submitted, significantly outsell LHF and Chalmers tofu where ranged, as highlighted in Table 3 below. The strength of this product performance provides Hings and Check with outstanding scaling opportunities. As noted below, the cost of scaling is far less than the Commission assumes.

⁶ SOI at [56.2]

[REDACTED]

- 5.4 [REDACTED] suggests that the Hings and Check offers have strong consumer appeal which represents significant potential for growth.
- 5.5 As shown in the Table 4 below, an analysis of Hings and Checks potential volume, shows if [REDACTED]. Pak'n Save North Island currently accounts for [REDACTED]% of Tofu sold in the major supermarket chains, so opportunities would also exist to extend ranging in other accounts.

[REDACTED]

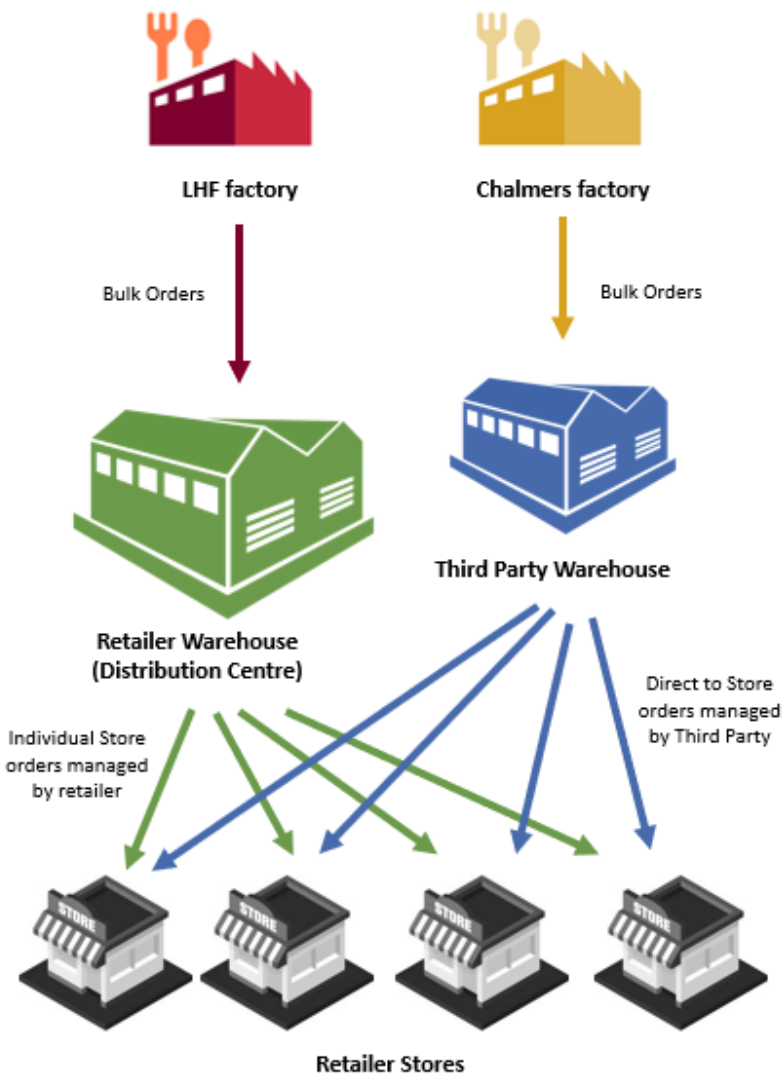
- 5.6 As previously submitted, Asian Supermarkets carry a very wide range of tofu products. Suppliers such as Best Food (<http://www.bestfoodfreshtofu.co.nz/>) could also be well placed to scale up to supply the major supermarket chains. Best Foods provides a significantly larger range than LHF or Chalmers (11 tofu products are featured on their website: <http://www.bestfoodfreshtofu.co.nz/#our-products>). This is counter to the initial Commerce Commission finding that smaller suppliers have a more limited range of products.⁷
- 5.7 As the cost of equipment to build scale is quite modest the investment required to boost production by Hings, Check or Best Food would not be excessive. By way of example the current book value of the Chalmers tofu equipment is [REDACTED]. This level of investment is modest and quite manageable and financeable for a small entity who can show a contract to supply a major retailer. Equipment could easily be accessed through equipment financing. Further, debtor factoring of working capital would also provide additional cashflow support. The incremental capital that an entity needs to find themselves would be limited.
- 5.8 Table 5 below (as previously submitted) shows the manufacturing equipment required to produce tofu and includes notes on costs and Chalmers references in relation to their equipment investments:

[REDACTED]

- 5.9 The logistics network to support expansion is also not a significant constraint. New Zealand is well served by an established network of third party brokers and distributors, who carry out store level sales and merchandising, warehousing stock, pick, pack and deliver orders direct to store, or to retailer DC's, on a percentage of sales fee basis. Utilising third parties for logistics requires no capital outlay and provides a clear pathway to rapidly expand to a wider store network.

⁷ SOI at [58.2]

5.10 The direct to store and retailer warehousing approaches are illustrated in the diagram below:



5.11 LHF does not believe, as the Commission contends,⁸ that smaller market participants carry significantly higher logistics costs than established players. Chilled distribution is an expensive requirement for all players in the market and synergies from larger scale are limited.

5.12 The relative costs of LHF’s (via Retailer DC) and Chalmers (via Third Party direct to store) is shown in Table 6 below:

[redacted]⁹

5.13 It should be noted that logistics costs account for a low percentage of cost of sales (ie approximately [redacted]%) and even if costs were higher they would not result in a materially different overall gross margin outcome.

5.14 To LHF’s knowledge, all New Zealand tofu manufacturers, including LHF and Chalmers source soybeans (the key raw material from which tofu is made) from commodity importers such as Davis Food Ingredients (<https://davis.nz/about-us>). Soybeans are a global commodity and prices fluctuate depending on global demand, annual crop results in major growing regions and supply disruptions. Due to the modest volumes required to supply the New Zealand market (relative to global demand), no New Zealand manufacturers (including LHF and Chalmers) have enough scale to purchase direct

⁸ SOI at [58.1]

⁹ [redacted]

from growers at preferential prices and are therefore price takers. Contrary to the Commission's preliminary view¹⁰, there is no significant cost disadvantage to smaller tofu manufacturers.

6. 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

- 6.1 As previously advised, there are a significant number of new entrants to the plant-based foods market in New Zealand, including start-ups, existing food producers extending to plant-based and international players. Details of these are outlined in the Notification. Given tofu is a growing segment within the plant-based category, any current or future market participants could choose to expand into this segment.
- 6.2 As highlighted above, tofu manufacturing equipment does not carry significant investment requirements. In addition, unique packaging formats may not be required as vacuum sealed plastic film, typically used to pack tofu is also used on a variety of other product formats, including sausages and burgers.
- 6.3 Imported Australian made products are found in every aisle of New Zealand supermarkets and are a well-established and viable way to participate in the New Zealand grocery marketplace. Australia's plant-based food category include tofu with a number of manufacturers who supply grocery outlets. Macro, Woolworths NZ's Private Label range is manufactured in Australia and already established in New Zealand, selling at a competitive price, which, contrary to the Commission's preliminary view,¹¹ highlights the clear viability of sourcing from Australia.
- 6.4 Sydney based Nutrisoy (<https://www.nutrisoy.com.au/our-company>) would seem a very strong candidate to supply the NZ market. Their website notes they '*heavily engage in private label and contract manufacturing*' and already supply 'selected international markets'. They would be well placed to launch branded product (they already supply the largest branded product in Australian grocery, Soyco), contract pack on behalf of another plant-based participant, or expand private label offers to New Zealand retailers.
- 6.5 New Zealand market volume requirements are significantly lower than what is required to supply major Australian retailers Woolworths or Coles. Other Australian tofu manufacturers (including Australian Eat Well (Simply Better and Hakea brands) <https://www.australianeatwell.com.au/company>, Unigreen Foods (EverGreen brand and various Asian-style offerings) <https://evergreenfoods.com/about-us/> and King International (Kingland and Pureland brands) <https://www.kingintl.com.au/who-we-are>) would also be in a position to supply into New Zealand via their own brands or in partnership with others.
- 6.6 Other international markets could also expand their supply to New Zealand. By way of example, Californian supplier Morinaga (<https://morinaganutrition.com/pages/about-morinu-silken-tofu>) already supplies tofu products to both Woolworths NZ and Foodstuffs South Island under the Mori-Nu brand, with imminent scale to expand.
- 6.7 As previously submitted, LHF notes that a wide variety of tofu products from a number of international markets such as Korea, Japan and China are widely available in Asian Supermarkets. These suppliers may also have the capability to expand into major grocery.

7. WHETHER MAJOR GROCERY RETAILERS ARE LIKELY TO CONSTRAIN A TOFU PRICE INCREASE IN ANY OF THE FOLLOWING, OR ANY OTHER WAYS

- 7.1 Macro provides a useful case study on Private Label. Woolworths NZ launched Macro tofu in early 2019, including firm tofu and marinated variants. By February 2020, immediately prior to Covid, the entry of Macro had stimulated significant growth in Woolworths NZ tofu sales and Macro had secured [REDACTED].
- 7.2 The Covid period from March 2020 until early 2022 saw significant disruption to supply of grocery products, with Macro tofu imported from Australia experiencing stock delays and periods of out of stock

¹⁰ SOI at [59]

¹¹ SOI at [66.1]

due to the trans-Tasman line capacity and port handling capacity. This affected Macro in a similar manner to a myriad of other suppliers. Current expectations are that this is a short term situation that will progressively normalise from the middle of this year. Post Covid, with regular supply secured, LHF expects to see the growth in sales and share of Macro tofu return to early (pre COVID) 2020 trends.

7.3 In terms of the future potential of private label sales, the Australian market is a useful reference. Woolworths Australia (owner of Woolworths NZ) sells the same Macro tofu branded range that is supplied in New Zealand and has achieved significant market share in Australia. While LHF cannot disclose Woolworth Australia sales data (due to confidentiality obligations) retailer backed private label sales (which includes Woolworths and Coles) dominate the Australian market as shown in Table 7 below:

[REDACTED]

7.4 In Woolworths Australia, LHF understands only Macro, Evergreen and Made with Plants tofu products are available and the private label share of tofu is higher than in Coles, where a wider range of brands is available.

7.5 Shelf space allocations are a useful proxy for market share. An analysis of a typical Woolworths shelf fixture shows that in this store, Macro tofu and tempeh dominates the allocated shelf spacing, accounting for 13 of the 15 tofu and tempeh shelf facings as show below. This represents 87% of the tofu and tempeh facings allocated to Macro products within the plant-based ingredients section of the store:



Source: Woolworths Tuggerah, Central Coast, NSW – photo taken 27 March 2022

7.6 As retailers utilise private label product to build points of uniqueness vs their retail competitors and to enhance profitability, it is highly likely Woolworths New Zealand will consider taking a similar strategy to Woolworths Australia, expanding the shelf facings and priority given to Macro tofu and reducing emphasis on branded product such as the products from Bean Supreme and Tonzu.

7.7 This may include extending the range of Macro tofu sold in New Zealand. Table 8 below highlights there are a number of varieties of Macro Tofu currently sold in Australia, that are not yet available in New Zealand, which could be added to their local range. Woolworths Australia also sell several Tempeh varieties under the Macro brand which could also be launched into New Zealand.

[]

- 7.8 An additional consideration on the potential of Private Label relates to Foodstuffs recent launch in late 2021 of Pams Tofu as part of a large range of plant-based food offerings, comprising 15 individual variants in total across chilled and frozen foods.
- 7.9 For the quarter to 13 March 2022, Pams Tofu Firm 450g is now available in []% of all Pak'n Save and New World stores nationally and is now ranked within the [] selling tofu product variants in these stores. LHF expects store ranging, sales volumes and rankings to continue to climb over the coming months as Foodstuffs continues to build up this new range. Once firm tofu is established, we would expect Foodstuffs to extend the Pams range to flavoured and possibly silken tofu products.

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

- 7.10 Retailers can also use ranging decisions and shelf space allocations to provide preferential positioning for private label products and encourage entry and expansion of new and smaller players. This occurs both at store level, particularly in Foodstuffs stores, where owner operators have some discretion to support local or niche brands and at national account level where ranging decisions are made across multiple stores.
- 7.11 The history of both Bean Supreme and Chalmers reflects this expansion path, with both starting out supplying health food specialist stores initially and over time extending to selected grocery retail stores and eventually nationwide across all major supermarkets.
- 7.12 More recently Plant-Based startup Sunfed secured retailer support to expand, despite supply challenges, to now be well established across all major retailers and extending from their initial Chicken-style product to Bacon and Beef-style offers.
- 7.13 Another well published example is the development of Pics Peanut Butter which was encouraged by retailers to enter the existing market, dominated by larger brands Kraft, Eta and Sanitarium. This was initially in the Nelson region, then into mainstream supermarkets, securing preferential shelf position. Pics is now the clear #1 brand in this category.
- 7.14 It is likely that one or more of the major retailers would encourage an existing or new tofu supplier to expand by, providing ranging and preferential shelf space to grow, should they determine a need to constrain or reduce the merged entity's position.

reducing shelf space or promotional slots, or deleting SKUs

- 7.15 Retailers determine ranging decisions, shelf space allocations and promotional slots at their discretion. This can be used to reduce the dominance of major players, as recently occurred in the well published reduction on Sealord frozen fish range by Foodstuffs North Island. As previously noted, in a media release, Foodstuffs stated that Sealord's "...offered two proposals through the range review process. The first of these had a number of conditions attached, one of which would have resulted in increased average retail prices to our customers. This fell short in providing a competitively priced offer to our customers and was not a scenario we could accept. An alternate proposal was also made by Sealord, which we accepted and in doing so we were transparent in regards to the ranging we could provide in return." Sealord has stated that the outcome of the review is a 50-80% reduction in the products it sells through Foodstuffs. It is understood that the intent is to replace these products with a new range of frozen products.

Sources: <https://www.foodstuffs.co.nz/news-room/clearing-up-a-fishy-tale>,
<https://www.stuff.co.nz/business/industries/126670095/uncertainty-for-sealord-as-contract-slashed-by-foodstuffs-north-island>.

- 7.16 LHF regards the countervailing power of the supermarkets as a significant constraint on the merged entity and notes this is consistent with the conclusions of the recent Commerce Commission study into New Zealand supermarkets. As noted by the Commission chair "*many grocery suppliers fear having their products removed from store shelves if they do not accept some costs, risks and contractual*

*uncertainty. This can reduce the ability and incentive for suppliers to invest and innovate, reducing choice for consumers”.*¹²

parallel importing other brands

- 7.17 LHF does not regard parallel importing as likely for tofu, given this is a chilled product, requiring close management of shelf life and product quality and integrity.
8. **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.**
- 8.1 As explained at 2.3 and previously submitted, tofu and plant-based meat alternatives are sold in the same section of stores with high levels of shopping across product sub-segments and animal protein options.
- 8.2 The breadth of range available, shelf space allocated as well as price and promotional attractiveness of tofu relative to other plant-based alternatives will clearly constrain the volume of tofu sold. As discussed in earlier sections, all plant-based products and animal protein solutions are competing for the same limited number of weekly protein meal occasions at home for which shoppers purchase.
9. **TRADING RELATIONSHIPS INDEPENDENT OF SANITARIUM**
- 9.1 The Commission implies¹³ there may be coordination between LHF and Sanitarium in relation to their respective product lines. This concern has no foundation.
- 9.2 While LHF and Sanitarium have common owners, each is a separate legal entity operating independently of the other. There is no cross over in trading relationships with retailers. LHF and Sanitarium supply different product categories under separate and unrelated trading terms.

¹² NZCC media release

¹³ SOI at [71]