

Reward Supply Co Pty Limited / Southern Hospitality Limited

Joint submission in response to Commerce Commission’s Statement of Issues

A. Summary of submissions

1. Reward Supply Co Pty Limited (**Reward**) and Southern Hospitality Limited (**Southern Hospitality**) make this joint submission in response to the Commerce Commission’s Statement of Issues.¹
2. The parties agree with the Commission’s conclusion that the acquisition is unlikely to substantially lessen competition in relation to smallware or consumables,² or due to coordinated effects.³ The parties have not provided any further submissions on these issues.
3. The outstanding issues concern whether the Commission can be satisfied that the acquisition will not substantially lessen competition for the supply of commercial kitchen equipment – resold by the parties either standalone or as part of a “project” – due to unilateral⁴ or vertical effects.⁵
4. The parties disagree with the Commission’s view that it cannot be so satisfied based on the information before it. That said, the Commission has expressed several findings that the parties agree with, namely that:
 - 4.1 the relevant counterfactual is the status quo;⁶
 - 4.2 there are many firms that compete with the parties to supply commercial kitchen equipment⁷ (the parties understand the Commission has spoken to 11 competing resellers, which the Commission says are not all the resellers present in the New Zealand market⁸);
 - 4.3 barriers to entry to the markets are low;⁹
 - 4.4 large customers have countervailing power through the ability to import equipment or acquire equipment directly from manufacturers;¹⁰ and
 - 4.5 if there is a separate “project” market, the acquisition results in modest market share aggregation that is within the Commission’s concentration indicators.¹¹
5. The parties also agree with the Commission that the key question is whether the merged firm would be constrained from profitably increasing prices above the levels that would prevail without the merger.¹²
6. The Commission has expressed scepticism that the merged firm would be constrained and, in particular, about the likelihood of competitors expanding to a sufficient extent to constrain the merged firm.¹³ The parties say this scepticism is misplaced and inconsistent with the evidence before the Commission and orthodox antitrust analysis.

¹ Confidential information in this submission is contained in bolded square brackets and highlighted in yellow (i.e., **[CONFIDENTIAL]**).

² Statement of Issues, at [11.1].

³ Statement of Issues, at [11.2].

⁴ Statement of Issues, at [7].

⁵ Statement of Issues, at [10].

⁶ Statement of Issues, at [59].

⁷ Statement of Issues, at [76] and [100].

⁸ Statement of Issues, at [74.1].

⁹ Statement of Issues, at [83], [103], and [114].

¹⁰ Statement of Issues, at [88] and [107].

¹¹ Statement of Issues, at [95].

¹² Statement of Issues at [65], [78], and [104].

¹³ Statement of Issues at [65], [78], and [104].

7. Stepping back, this is not a complicated market. The reselling of commercial equipment is neither difficult nor complex. Reselling equipment simply involves acquiring equipment manufactured by others and then reselling that equipment to customers.
8. The parties' view remains that there is nothing to prevent any of their existing rivals from expanding sales in the event the merged firm sought to increase prices from the levels that would prevail without the merger. Furthermore, manufacturers have strong incentives to ensure that competition between resellers remains strong and to prevent the merged firm gaining market power.
9. The parties make five points in relation to the Commission's view that there may be barriers to expansion (warehouses, showrooms, and reputation) that would prevent competitors expanding to constrain the merged firm.
 - 9.1 First, based on the Commission's theory of harm and market share estimates, the extent of expansion required to replace any competition lost through the merger is modest on a national basis, and even smaller on a regional basis. And while the Statement of Issues cites possible barriers to expansion, those "barriers" could be overcome quickly – and certainly within the two years usually adopted for the LET test – without material sunk capital investment.
 - 9.2 Second, to the extent that warehouse space is required to compete to sell equipment:
 - 9.2.1 existing rivals have already overcome this hurdle and there is no evidence cited in the Statement of Issues that existing competitors are capacity constrained by their current premises;
 - 9.2.2 the evidence shows that all parties can and do supply across the country from their existing warehouses, or by selling products which are supplied directly from a manufacturer's warehouse; and
 - 9.2.3 if an existing competitor needed to invest in new warehouse space to expand sales, that investment would not involve material sunk costs. A warehouse is not a specialised asset as evidenced by the plethora of warehouses in markets across the economy. As the Commission has recognised in its Merger Guidelines, the lower the sunk costs, the lower the risk faced by the person contemplating expansion and the less likely that any need for such investment will impede expansion.¹⁴
 - 9.3 Third, there is no evidence that showrooms are necessary to compete to sell commercial equipment. The evidence is the opposite. In any event, the overlap in the parties' showrooms is limited to the main centres, where other rivals or manufacturers have showrooms. Moreover, as with warehouse space, any investment in showroom space would not involve material sunk costs.
 - 9.4 Fourth, there is very limited evidence to support the contention that reputation is a barrier to expansion in the projects market. The Statement of Issues presents one statement from one reseller in relation to one type of customer. The Commission cannot infer anything from that isolated statement. Conversely, the marketplace evidence is that resellers can and/or do supply all types of project customers.
 - 9.5 Fifth, the evidence from manufacturers is that they do, and will continue to, price and set other terms to promote a competitive reseller market. It is not in any manufacturer's interest to allow competition between resellers to diminish or market power to emerge. If faced with that possible scenario, manufacturers will have every incentive to support another reseller to expand.

10. The constraint from existing competitors and the countervailing power manufacturers hold, should be sufficient to satisfy the Commission that no substantial lessening of competition is likely.
11. However, the Commission has also underestimated the countervailing power possessed by all customers, not just large customers. As Reward has told the Commission, the rationale for the acquisition is to improve the merged firm's consumables and smallware business, markets which the Commission has found are competitive.
12. If the merged firm sought to increase equipment prices, that strategy would undermine the very rationale for the acquisition as customers who felt they paid too high a price in the equipment market, would simply express their frustration by not using the merged firm for smallware and consumables. This is a powerful source of countervailing power for customers of all sizes that is not referenced in the Statement of Issues.
13. Finally, the parties submit that to the extent the Commission's theory of harm is based on the merged firm gaining access to better terms from manufacturers, manufacturers will have no incentive to set terms in a way that reduces reseller competition (e.g., by setting terms that do not enable smaller resellers to compete). Moreover, lower input costs will lower the merged firm's profit maximising price. Put another way, there will be efficiencies which will be passed through to customers that are relevant to the Commission's assessment.¹⁵
14. For all these reasons, the parties submit that based on the Commission's findings to date, the practical evidence before the Commission, and orthodox antitrust analysis, the Commission should grant clearance. Indeed, the parties submit that there is no reasonable basis on which the Commission can decline clearance.
15. The remainder of this submission is structured as follows:
 - 15.1 Section B provides comment on the legal framework the Commission is required to follow;
 - 15.2 Section C explains why the Commission can be satisfied that the acquisition is unlikely to substantially lessen competition in relation to the sale of standalone equipment;
 - 15.3 Section D explains why the Commission can be satisfied that the acquisition is unlikely to substantially lessen competition in relation to the sale of equipment as part of a "project"; and
 - 15.4 Section E explains why the Commission can be satisfied that the acquisition is unlikely to result in vertical effects.

B. Comment on the legal framework

16. The parties accept that the Commission's investigation is ongoing. Nevertheless, the parties make the following observations on the legal framework the Commission must apply.
17. The focus of the substantial lessening of competition test is on the change resulting from the acquisition, not what level of competition may or may not exist in a market.¹⁶ Moreover, as the Australian Federal Court has cautioned:

¹⁵ Merger Guidelines at [3.122]-[3.123].

¹⁶ *Air New Zealand/Qantas v Commerce Commission (No 6)* (2004) 11 TCLR 347 (HC) at [42].

... it is not for the ACCC or this Court to engineer a competitive outcome. The only question for this Court is whether the merger would have the effect, or be likely to have the effect, of substantially lessening competition in the [relevant market].¹⁷

18. It is axiomatic that the Commission's assessment must be based on the practical evidence available to the Commission.¹⁸ The Commission's assessment cannot be based on theory or speculation alone and, in the parties' submission, should reflect the weight of evidence rather than isolated opinions which are not supported by other evidence.
19. The parties accept that they are required to satisfy the Commission that the acquisition is unlikely to substantially lessen competition in any market. However, the Commission must make its assessment on the balance of probabilities. A hypothesis (here, that a substantial lessening of competition is unlikely) is proven on the balance of probabilities if it is more probable than the competing hypothesis.¹⁹
20. While the Commission is entitled to decline clearance if it is in "doubt" as to whether a substantial lessening of competition is likely, "doubt" does not mean "beyond reasonable doubt" as used in the criminal context. Rather, as the Court of Appeal has emphasised in the clearance context, "doubt" simply means an applicant failing to discharge the burden of satisfying the Commission, on the balance of probabilities, that no substantial lessening of competition is likely.²⁰
21. In summary, the Commission should not base its assessments on theoretical concerns not backed by evidence, and nor should it seek or require a level of certainty or precision in the evidence that is unattainable. It should look to the weight of evidence it has received from the parties and the 36 third parties the Commission has interviewed and make its assessment on that basis.
22. The Australian Federal Court has described the task of a regulator in the Commission's position when assessing whether a substantial lessening of competition is likely as follows (emphasis added):

The meaning of "likely" reflecting a "real chance or possibility" does not encompass a mere possibility. The word can offer no quantitative guidance but requires a qualitative judgment about the effects of an acquisition or proposed acquisition. **The judgment it requires must not set the bar so high as effectively to expose acquiring corporations to a finding of contravention simply on the basis of possibilities, however plausible they may seem, generated by economic theory alone.** On the other hand it must not set the bar so low as effectively to allow all acquisitions to proceed save those with the most obvious, direct and dramatic effects upon competition. By the language it adopts and the function thereby cast upon the Court and the regulator in their consideration of acquisitions s 50 gives effect to a kind of competition risk management policy. **The application of that policy, reflected in judgments about the application of the section, must operate in the real world. The assessment of the risk or real chance of a substantial lessening of competition cannot rest upon speculation or theory.** To borrow the words of the Tribunal in the Howard Smith case, the Court is concerned with "commercial likelihoods relevant to the proposed merger". **The word "likely" has to be applied at a level which is commercially relevant or meaningful as must be the assessment of the substantial lessening of competition under consideration...**²¹

C. No substantial lessening of competition in relation to the sale of equipment on a standalone basis

23. There is no dispute that the parties compete to sell commercial kitchen equipment. Moreover, as described in Section A, there are many areas in which the parties agree with the Commission's findings as expressed in the Statement of Issues, namely:

¹⁷ *Vodafone v ACCC* [2020] FCA 117 (*Vodafone*), at [11].

¹⁸ *Commerce Commission v Woolworths* [2008] NZCA 276 (*The Warehouse*) at [191].

¹⁹ *Commerce Commission v Woolworths* [2008] NZCA 276 (*The Warehouse*) at [99].

²⁰ *The Warehouse* at [98].

²¹ *Vodafone* at [52].

- 23.1 there are many firms that compete with Reward and Southern Hospitality to supply commercial kitchen equipment;²²
- 23.2 barriers to entry are low,²³ which is aptly illustrated by Australian reseller Euroquip's imminent entry into the New Zealand market (discussed further at [87] to [89] below); and
- 23.3 large customers have countervailing power.²⁴
24. The parties also agree that the question for the Commission is whether, post-acquisition, the merged firm would be able to increase prices above the levels that would prevail without the merger without facing constraint from existing rivals expanding and/or manufacturers and customers exercising countervailing power.²⁵ It is the answer to that question where the parties differ from the Commission.
25. The Statement of Issues expresses scepticism about rivals' abilities to expand because:
- 25.1 an existing competitor may need to develop and operate showrooms and warehousing in different regions to be able to effectively secure customers; and
- 25.2 the incentives to make those investments may be limited by the ability of smaller resellers to obtain supply terms that allow them to compete.²⁶
26. For the reasons explained in this section, the evidence before the Commission and standard antitrust analysis does not support the hypothesis that existing rivals would be constrained from expanding in this way (or any other way). In addition, this section explains why the Commission has underestimated the level of countervailing power that exists.

Comments on the correct approach to assessing expansion

27. The parties make two initial points about the Commission's assessment of the likelihood of expansion in this market.

The extent of expansion required

28. First, the level of expansion only needs to be sufficient to constrain the merged firm from increasing prices above current levels. It follows that based on the Commission's theory of harm, a rival would not need to expand to match the merged firm's market share; rather, at most, the existing competitor would need to be able to expand to replace the constraint Reward currently imposes on Southern Hospitality.
29. The Statement of Issues records the Commission's estimate that the merged firm's market share would be 60% nationally (Southern Hospitality, 45%, and Reward, 15%). The Statement of Issues also states that the merged firm's share would be "particularly high outside of Auckland"²⁷ without providing any information to support that proposition.
30. The Commission has rightly issued a health warning as to the accuracy of those market shares.²⁸ The Commission's estimates do not correlate with the parties' view of their own market shares. Furthermore, it is not clear on the information provided to the parties whether the market shares the Commission has calculated compare like with like or would include all sales. For example:

²² Statement of Issues, at [76].

²³ Statement of Issues, at [83] and [114].

²⁴ Statement of Issues, at [88].

²⁵ Statement of Issues, at [78].

²⁶ Statement of Issues, at [85].

²⁷ Statement of Issues, at [73].

²⁸ Statement of Issues at footnote 54.

- 30.1 Southern Hospitality includes items such as hand blenders and microwaves as equipment. These items account for a significant portion of Southern Hospitality's sales and are sold by many non-commercial kitchen resellers (e.g., Briscoes, The Warehouse, etc) to the same customers as the parties but whose sales would not be included in the Commission's market share estimates.
- 30.2 Similarly, for some types of large equipment, such as commercial refrigeration, there are specialist competitors (e.g., Interfridge²⁹, Honar³⁰, and CoSell³¹) who sell commercial refrigeration to the same customers as the parties but would not be included in the Commission's market share estimates.
31. For these reasons and given the Commission has not spoken to all resellers, on any view, the Commission's shares should be treated as a "worst case" market share scenario.³²
32. In any event, even applying the Commission's theory of harm, the Commission's own market share estimates imply that an existing competitor would only need to expand to, at most, a 15% share on a national basis. At that point, the rival should be enjoying any cost and scale advantages assumed to be enjoyed by Reward.
33. If looked at on a regional basis, the extent of expansion that would be required is likely to be even lower given the aggregation of market share caused by the merger will be lower. To the extent the merged firm's post-acquisition share would be higher outside Auckland, this is due to Southern Hospitality's higher existing market share outside Auckland. Conversely, Reward's market share outside Auckland is lower than it is in Auckland. Indeed, Reward expects that it is unlikely it would be the second largest supplier in many regions of New Zealand.
34. This has two implications for the Commission's theory of harm.
- 34.1 First, if Reward is not the second largest provider in a region and the markets are regional, then applying the Commission's theory of harm, Reward should not be the firm constraining Southern Hospitality in that region.
- 34.2 Second, and in any event, the extent of expansion needed to replace the constraint Reward currently provides in any region is likely to be lower than the expansion needed on a national scale.

Expansion does not need to happen overnight

35. Second, as is made clear in the Commission's Merger Guidelines, expansion does not need to happen immediately. Rather, the correct approach is to ask whether sufficient expansion is likely to occur within two years of a price increase.³³ If it would, then a substantial lessening of competition is unlikely.
36. The Statement of Issues addresses neither the extent of expansion required, nor the timeframe in which it could occur. As explained below, any rival could expand market share quickly – and certainly within two years – without having to make the capital investments the Commission posits. And even if capital investments were necessary, the expenditure would not be sunk (see [46.2], and [65] to [66] below).

The need for warehouse space to expand into different geographic regions

37. The Statement of Issues presents a hypothesis that an existing competitor may need to invest in a new warehouse in a region to expand in that region. There is no evidence cited in

²⁹ www.interfridge.co.nz

³⁰ www.honar.co.nz

³¹ www.cosell.co.nz

³² Statement of Issues, at [74.1].

³³ Merger Guidelines at footnote [95].

the Statement of Issues to support this hypothesis. Indeed, based on the Statement of Issues none of the 11 competitors the Commission has interviewed appears to have raised the need for new warehouses as a factor that would prevent them expanding.

38. For the reasons outlined below, existing competitors will not be constrained from expanding by a need to invest in warehouses.

No evidence that resellers are capacity constrained

39. To the extent that warehousing is important, all existing participants will have warehousing arrangements in place. There is nothing in the Statement of Issues to suggest that any of these competitors face capacity constraints that would prevent them selling more equipment.

40. The likely lack of capacity constraints is illustrated by the fact that equipment is unlikely to take up a large part of a warehouse. The bulk of a warehouse will comprise smallware and consumables. For example:

40.1 only [CONFIDENTIAL]% of Southern Hospitality's Tauranga warehouse, and [CONFIDENTIAL]% of Southern Hospitality's Christchurch warehouse is used to stock equipment (mostly Southern Hospitality's own brand of refrigeration, Delta, which Southern Hospitality imports³⁴); and

40.2 even Reward, which is almost exclusively an importer and is the distributor for Rational ovens, has only [CONFIDENTIAL]% of its Auckland warehouse used to stock equipment.

No requirement for multiple warehouses

41. The evidence also shows that multiple warehouses are not needed in order to supply to anywhere in New Zealand, meaning distribution can occur from one central warehouse. For example:

41.1 while Reward has a 3PL warehousing arrangement in Christchurch, Reward distributes all its equipment nationwide from its Auckland warehouse;³⁵

41.2 to the extent that Southern Hospitality holds and distributes equipment (primarily refrigeration), this is primarily done from its Tauranga Distribution Centre with the Christchurch warehouse operating as a satellite;³⁶ and

41.3 other resellers have told the Commission they supply throughout New Zealand today.³⁷

Continued ability of resellers to sell ex-manufacturer reduces the need for warehousing

42. The fact that significant volumes of equipment can be and are distributed directly from manufacturers to customers (removing potential double handling), further obviates the need for investment in multiple warehouses to compete. Ex-manufacturer and ex-warehouse deliveries take the same amount of time, so there is no time penalty in an ex-manufacturer model.³⁸

43. Southern Hospitality estimates that [CONFIDENTIAL]% of the equipment it sells is delivered ex-manufacturer. While Reward's business model is different as it is primarily an

³⁴ Other resellers that import their own brand of refrigeration include Skope, Nisbets, Electrolux, Stoddarts/Wildfire, Euroquip and FED. There are also several competitors that specialise in the sale of commercial refrigeration including Interfridge, Honar, and CoSell.

³⁵ See Clearance Application at [45].

³⁶ See Clearance Application at [45].

³⁷ Statement of Issues, footnote 36.

³⁸ Very urgent (i.e., immediate) orders are extremely rare.

importer and so distributes most equipment from its warehouse, the Southern Hospitality model shows that there is a viable business model where most product is distributed ex-manufacturer.

44. The ability for resellers to sell product ex-manufacturer is likely to increase in the future. Indeed, the parties are aware that **[CONFIDENTIAL]**.

Investment in warehouse capacity would not be sunk

45. In summary, what the evidence indicates is that existing competitors already supply nationwide from their existing warehouses, and there is no evidence to suggest they could not expand their sales further, both in terms of reach and scale.
46. However, even if a competitor decided they needed new warehousing space, that would not require significant sunk capital investment.
- 46.1 First, significant capital investment may not be needed. There are numerous 3PL providers providing warehousing and logistics services throughout New Zealand. A competitor could utilise such a provider – as Reward does in Christchurch – to add additional warehouse capacity without significant capital investment.
- 46.2 Second, even if a competitor decided to invest capital and build or acquire a warehouse, that investment would not be sunk. Any warehouse would not be specialised and could be easily deployed for another purpose, reducing the riskiness of that investment, and meaning it is unlikely to impede expansion.
47. For all these reasons, existing competitors will not be constrained from expanding by a need to invest in warehouses.

The need for a competitor to have showrooms to expand into different geographic regions

48. The Statement of Issues contains little evidence to support the hypothesis that a competitor would need to build showrooms to expand into new regions. Indeed, it is notable that the Statement of Issues does not cite any of the resellers it has interviewed as saying that having showrooms is important to competition.
49. For the reasons explained below, existing competitors will not be constrained from expanding by a need to invest in showrooms.

Evidence cited in the Statement of Issues does not support a conclusion that showrooms are an important aspect of competition

50. The only evidence presented in the Statement of Issues to support the proposition that showrooms are important to competition are statements made by three customers.³⁹
- 50.1 The first customer is reported to have said a showroom “was helpful, especially when doing something different or trying to imagine something in a space”.
- 50.2 The second customer is reported to have said they sometimes want to look at “bigger stuff”, although it is not clear from the Statement of Issues that the customer is referring to equipment.
- 50.3 The third customer is reported to have said that when it receives quotes, it considers where it can look at equipment.
51. These isolated statements of three customers’ (weak) preference does not support a conclusion that having local showrooms is an important factor in these customers’ purchasing decisions, let alone an important driver of competition across the market.

³⁹ Statement of Issues, footnote 37.

Statement of Issues conflates two customer decision points

52. In reaching the view that showrooms may be a barrier to expansion, the Statement of Issues errs by conflating two issues:
- 52.1 a customer wanting to look at equipment (i.e., deciding what type of product to buy); and
- 52.2 a customer's decision as to who to buy that product from.
53. These two decisions are separate, and this has important implications for the Commission's analysis.
54. This market does not operate like a supermarket or a consumer electronics or whiteware retailer with physical stores in high traffic areas selling to consumers. No commercial kitchen equipment is sold through showrooms. All sales occur remotely, whether online via a website, or by customers making direct contact with suppliers either by phone or email.⁴⁰
55. Moreover, the customer is very different. A commercial kitchen equipment reseller is a B2B retailer selling to sophisticated, informed, and knowledgeable customers. Indeed, customers work with commercial kitchen equipment daily and do not, generally, need to physically see the equipment before making a purchasing decision. Southern Hospitality estimates only [CONFIDENTIAL]% of customers it has sold equipment to visit a showroom for the purpose of viewing equipment.
56. In the parties' experience, to the extent that customers value a showroom, the value is in relation to smallware not equipment. Customers can want to see and touch crockery and glassware etc. That same impetus does not apply for equipment.
57. Perhaps the best evidence of the lack of importance of a showroom are the dual facts that resellers:
- 57.1 display only a handful of equipment products in their showrooms;⁴¹ and
- 57.2 devote little space to its display. For example, only [CONFIDENTIAL] in Southern Hospitality's Auckland showroom is devoted to displaying equipment, and only [CONFIDENTIAL] in Dunedin.
58. Simply put:
- 58.1 a customer does not walk into a showroom to buy commercial kitchen equipment. Purchases are made remotely; and
- 58.2 in the rare situations where a customer may decide to view a product, they will then seek competing quotes on that same product from various resellers.
59. Seen in this light, far from being an advantage, running multiple showrooms risks other competitors free riding. Indeed, Southern Hospitality has been told by one of its competitors that where a customer wishes to view an item, the competitor tells the customer to go to the Southern Hospitality showroom to view the item, and then come back to the competitor for a price.⁴²

Showrooms are not standalone but part of other premises

⁴⁰ Clearance Application, at[44].

⁴¹ For example, Southern Hospitality only displays combi ovens in Auckland, Wellington, and Christchurch. More generally, in its largest showroom in Auckland, Southern Hospitality displays only [CONFIDENTIAL] large equipment items out of the [CONFIDENTIAL] large equipment items it sells, while in a smaller showroom such as Nelson, it displays [CONFIDENTIAL] large equipment items.

⁴² Similarly, if a customer is in an area where a competitor does not have a showroom, that competitor could tell the customer where they can view the equipment being used in a kitchen in that area.

60. The parties accept that many competitors in the market have showrooms. However, that does not indicate that showrooms are important to competition.
61. To the best of the parties' knowledge, none of these showrooms are standalone. Rather, they are add-ons to existing space. All competitors need some office space for their people to work from or base themselves in, which is often collocated with that competitor's warehouse space. In those circumstances, it is close to zero marginal cost for a competitor to have a showroom as part of an office/warehouse space.
62. This is exactly the reason why Southern Hospitality maintained showrooms despite closing its cash and carry operations. Southern Hospitality needed space for its staff and so there was almost zero marginal cost in having a display showroom as part of that space (with, in many cases, the showroom only open by appointment).

Overlap between showrooms is limited

63. In any event, the overlap in the parties' showrooms is limited to:
- 63.1 Auckland, where Nisbetts, Rollex, LKK, Aitkens, Wildfire, Mata Hospitality, Savebarn, Commercial Catering Equipment, JL Leonard, Chefs Compliments, Harvey Norman Commercial, and Stoddarts have showrooms, while Euroquip are about to open a showroom, and Moffat have a showroom for their products;
- 63.2 Hamilton, where Brian Millen, and Harvey Norman Commercial have showrooms and customers can easily access showrooms in Auckland and Food Equipment NZ's showroom in Rotorua;
- 63.3 Wellington, where BCE (Paraparaumu), Rollex, Hardy Trade Supplies, and Harvey Norman Commercial have showrooms; and
- 63.4 Christchurch, where Aitkens, Total Food Equipment, Catering Hardware Ltd, Head Chef, Tiger Hospo Equipment (more of a warehouse), and Harvey Norman Commercial have showrooms, and Moffat have a showroom for their products.
64. In short, the acquisition is unlikely to materially reduce any consumer's ability to view product in these regions.

Investment in showrooms would not be sunk

65. Finally, as with investment in warehouses, if a competitor wished to invest in a showroom that investment would not be sunk.
66. A showroom would not be specialised and could be easily deployed for another purpose. This is particularly so given that, on the Commission's theory of harm, the showroom would be in a place that could service the Auckland, Wellington, and Christchurch markets. As described earlier, the lack of material sunk costs reduces the riskiness of that investment.
67. For all these reasons, the parties submit that existing competitors will not be constrained from expanding by a need to invest in showrooms.

Relevance of better supply terms

68. The Statement of Issues contains little information to support the proposition that Reward and Southern Hospitality obtain better supply terms than their competitors. Moreover, while the Statement of Issues refers to the parties' competitors as being smaller scale, it does not:
- 68.1 provide any indication of the relative size of Reward as compared to other providers in this market; nor

68.2 refer to the fact that Nisbets is part of the Nisbets group, a multinational distributor which describes itself as “Europe’s largest catering supplies distributor”.⁴³

No incentive for manufacturers to allow market power to emerge by providing better supply terms to the merged firm

69. The only direct evidence about supply terms appears to be from the manufacturers who the Commission spoke to. The Statement of Issues records that:

The general feedback was that manufacturers considered they set their prices at a level that allowed smaller resellers to be competitive.⁴⁴

70. This feedback from manufacturers is consistent with what economic theory would say are manufacturers’ incentives. That is, manufacturers will be incentivised to ensure a competitive downstream reseller market to maximise their own profits when competing against other manufacturers at the wholesale level.

71. A manufacturer’s profitability depends on its wholesale price to the reseller and end customer demand. End customer demand depends on the reseller’s price, which is the wholesale price plus the reseller’s costs and mark-ups. As Carlton & Perloff note:

Every manufacturer, regardless of whether it is a monopoly or a competitive firm, wants its product distributed at the lowest possible costs. The manufacturer also wants the distributors to price and sell in a manner that is best for the manufacturer.⁴⁵

72. Manufacturers ultimately bear the effect of reseller mark-ups and high resale prices because they reduce demand for the manufacturer’s product. Furthermore, a reseller with market power in the resale market is also more likely to have market power in the buying market, allowing it to constrain wholesale prices.

73. Either way, market power at the reseller level will reduce a manufacturer’s profitability. This provides a strong incentive for manufacturers to maintain competition at the reseller level.

74. This incentive to maintain a competitive reseller market is consistent with manufacturers giving volume discounts to resellers. Volume discounts are a form of price discrimination enabling a manufacturer to increase demand for its products by reducing its average price to resellers who sell more, without also losing margin on other sales. Volume discounts can also give resellers an incentive to increase their efforts to sell the manufacturer’s product and can be used to pass on economies of scale to end consumers.

75. Importantly, a manufacturer needs to balance its desire to maximise resale volumes through discounts against the desire for a competitive downstream market. As explained above, it would not be profitable for a manufacturer to provide such generous volume discounts that a reseller gains market power due to its cost advantage.

76. However, not only is a manufacturer incentivised to prevent reseller market power, but they also have an incentive to prevent a reseller gaining increased negotiating power. A recent literature review by the OECD identifies that manufacturers have an incentive to reduce bargaining power by supporting the competitors of large resellers through lower wholesale prices.⁴⁶

Evidence suggests that all suppliers are price competitive at status quo levels

77. In any event, the question for the Commission is not whether other resellers can obtain terms as good as the merging parties. Rather, the question is whether they can compete on

⁴³ https://www.nisbets.co.nz/aboutus?cm_sp=NHP%20Footer_-_About%20Nisbets_-_About%20Us

⁴⁴ Statement of Issues, at [80.2.1].

⁴⁵ Dennis W. Carlton and Jeffrey M. Perloff, *Modern Industrial Organization* (Pearson 2015), p.438.

⁴⁶ OECD, *Purchasing power and buyers’ cartels*, 2022, p. 14.

price with the merged firm to the same extent that Reward can compete with Southern Hospitality today.⁴⁷

78. When asking this question, supply terms are only one factor that feeds into a firm's cost base. Different resellers will adopt different business models and this will impose different costs.
79. As explained in the Clearance Application, the parties do not understand Southern Hospitality to be a low-priced operator today due to its business model. Southern Hospitality currently operates 12 showrooms and employs a large sales force. This comes at a cost that other resellers avoid by operating from a lower cost base. This lower cost base would tend to mitigate if not eliminate, any supply advantage Southern Hospitality enjoys.
80. Without conducting a full review of all resellers' cost bases, the best the Commission can do is look to pricing outcomes. In this respect, the Statement of Issues refers to evidence from customers about pricing being "mixed", with one customer expressing the view the merged parties' prices were low, one expressing the view the merged parties' prices were high, and another saying Reward's prices were high.
81. To the extent the Commission is implying in the Statement of Issues that this "mixed" evidence means the Commission cannot reach any conclusions, the parties disagree. The "mixed" nature of the evidence illustrates that all parties are competitive on price at existing prices.
82. This is reinforced by the fact that there is evidence that all resellers can compete on price today even where they do not have a warehouse or a showroom. Recent examples the parties are aware of include:
- 82.1 In Auckland where Southern Hospitality and Reward have showrooms and Reward has a warehouse, **[CONFIDENTIAL]**;
- 82.2 In Hamilton, where Southern Hospitality and Reward have showrooms, **[CONFIDENTIAL]**;
- 82.3 In Tauranga, where Southern Hospitality has a warehouse and a showroom, **[CONFIDENTIAL]**;
- 82.4 In Matamata, where Southern Hospitality has a warehouse and a showroom in Tauranga, and a showroom in Hamilton, and Reward has a showroom in Hamilton, **[CONFIDENTIAL]**;
- 82.5 In the Central North Island, where neither party has a showroom or warehouse:
- 82.5.1 **[CONFIDENTIAL]**;
- 82.5.2 **[CONFIDENTIAL]**;
- 82.5.3 **[CONFIDENTIAL]**;
- 82.5.4 **[CONFIDENTIAL]**; and
- 82.5.5 **[CONFIDENTIAL]**;
- 82.6 In Wellington, where Southern Hospitality and Reward each have a showroom, **[CONFIDENTIAL]**;

82.7 In Christchurch, where Southern Hospitality and Reward each have a warehouse and a showroom:

82.7.1 [CONFIDENTIAL];

82.7.2 [CONFIDENTIAL];

82.8 In Queenstown Lakes, where Southern Hospitality has a showroom in Queenstown:

82.8.1 [CONFIDENTIAL];

82.8.2 [CONFIDENTIAL]; and

82.9 In Dunedin and Oamaru, where Southern Hospitality has a showroom in Dunedin:

82.9.1 [CONFIDENTIAL]; and

82.9.2 [CONFIDENTIAL].

83. What the Commission can conclude from the above is that the evidence is not consistent with the Commission's theory of harm.

To the extent the Commission believes the merged firm's terms of supply will improve, this will tend to reduce prices

84. Finally, to the extent that the Commission's theory of harm relies on the merged firm gaining access to better terms from manufacturers, the theory of harm must recognise that lower input costs will, all else being equal, lower the merged firm's profit maximising price. These purchasing efficiencies would benefit customers and the Commission should factor these into its assessment of competitive effects.⁴⁸

Manufacturer and customer countervailing power

85. While expansion by existing competitors will be sufficient to constrain the merged firm, the merged firm will also face constraint in the form of manufacturer and customer countervailing power.

Manufacturer countervailing power

86. The parties remain of the view that manufacturers can exert countervailing power for the reasons explained in paragraphs [97]-[98] of the Clearance Application and paragraphs [70] to [76] above. If the merged firm acted in a way that damaged demand for a manufacturer's products, the manufacturer would simply support another reseller to expand its sales or the manufacturer would increase its direct sales.

87. The imminent entry of Euroquip into the New Zealand market is an example of the countervailing power manufacturers can exert. Euroquip is an Australian reseller selling a range of commercial kitchen equipment (pizza ovens, conveyer ovens, bakery ovens, dough and pastry equipment, commercial refrigeration, and gelato machines).⁴⁹

88. In Australia, Euroquip resells Moretti Forni pizza ovens. Until recently, Southern Hospitality has resold Moretti Forni pizza ovens in New Zealand. Moretti Forni has informed Southern Hospitality that it will no longer sell to Southern Hospitality and will support Euroquip's entry into New Zealand. The reason for this is simply that Moretti Forni believes that Southern Hospitality is not selling enough Moretti Forni pizza ovens.

⁴⁸ Merger Guidelines at [3.122]-[3.123].

⁴⁹ <https://www.euroquip.com.au/>

89. Moretti Forni's actions illustrate that manufacturers could easily switch away from supporting a reseller such as the merged firm and would do so if they believed it was in their interests to do so.

All customers have countervailing power

90. The parties agree with the Commission that large customers can exercise countervailing power through their ability to obtain product.⁵⁰ The parties also accept that this option will be a less viable alternative for some customers.
91. However, the Statement of Issues overlooks the ability for all customers to exercise market power by leveraging competition in smallware and consumables.⁵¹ As Reward has told the Commission, the rationale for the acquisition is to improve the merged firm's consumables and smallware business. These markets are highly competitive.
92. If the merged firm were to seek to increase prices in relation to equipment, it would undermine the very rationale for the acquisition as customers who felt they paid too high a price in the equipment market, would simply express their frustration by not using the merged firm for smallware and consumables. This is a powerful source of countervailing power for customers of all sizes that is not reflected in the Statement of Issues.

D. No substantial lessening of competition in the "projects" market

93. The parties remain of the view that there is not a separate "projects" market in which design, equipment, supply, and installation (which are complementary products) are clustered into one market.⁵² The parties do not consider this is a valid competition law market. Nevertheless, the parties agree with the Commission that the precise market definition is less important than the Commission considering all relevant competitive constraints, and the extent of those constraints.⁵³
94. The parties also agree with the Commission that:
- 94.1 there are many firms that compete with Reward and Southern Hospitality (as a recent example, since the acquisition was announced, Metlifecare has asked Host Services to bid for projects);⁵⁴
 - 94.2 barriers to entry are low;⁵⁵
 - 94.3 large customers have countervailing power;⁵⁶
 - 94.4 if there is a separate "projects" market, the acquisition falls within the Commission's concentration indicators and involves modest market share aggregation.⁵⁷
95. Notwithstanding those views, the Commission has identified possible barriers to expansion by existing competitors.
96. The first potential barrier to expansion is that some smaller resellers say they obtain worse supply terms than the merging firms.⁵⁸ The parties repeat the submissions they have made in [68] to [84] above and make two further comments.

⁵⁰ Statement of Issues at [88].

⁵¹ Clearance Application at [101]-[102].

⁵² Clearance Application at [55]-[66].

⁵³ Statement of Issues at [33].

⁵⁴ Statement of Issues, at [100].

⁵⁵ Statement of Issues, at [83], [103], and [114].

⁵⁶ Statement of Issues, at [88] and [107].

⁵⁷ Statement of Issues, at [95].

⁵⁸ Statement of Issues, at [104.1].

- 96.1 First, it is not clear what the Commission means by “smaller resellers” in this context. As the Statement of Issues notes, there are several suppliers who are supplying equipment into large projects. None of these should be classified as a small reseller.
- 96.2 Second, and in any event, as the Statement of Issues records, “smaller resellers” have been able to overcome this factor (to the extent it exists),⁵⁹ indicating that it is not a factor that should impede expansion of an efficient competitor.
97. The second potential barrier to expansion is having demonstrable experience in a sector. As a general proposition, the notion that reputation is not a barrier to entry to the market as the Commission accepts,⁶⁰ but is a barrier to expansion appears inconsistent.
98. In any event, the only evidence cited in this regard is one statement by 1 of the 11 resellers that it has had difficulty winning government and institutional contracts, which it says was due to its lack of experience providing services to those types of customers.
99. As an initial point, government and institutional customers will be sophisticated procurers who would have the ability to exercise countervailing power, including through sponsoring new entry or expansion should they believe they are receiving an uncompetitive offer.
100. More specifically, the Commission cannot know whether a lack of experience was, in fact, a key determinant of that reseller not winning those contracts without interrogating each of them. However, what the Commission does know is that the concern was raised by only 1 reseller and in relation to only one type of customer.
101. The Commission cannot extrapolate from that single reseller’s view on why it did not win contracts that reputational effects act as a barrier to expansion and it would be unsafe for the Commission to do so.
102. Indeed, there are numerous examples of firms “expanding” to service customer types they have not typically supplied. Recent examples are:
- 102.1 Hostservice Commercial designing and supplying the prestigious INEOS Team UK Americas Cup Base in the viaduct harbour in Auckland delivering, various restaurants, and a kitchen design for Waitemata DHB;
- 102.2 Rollex Group winning projects for Wellington Hospital and Waikato Hospital; and
- 102.3 BCE supplying the Wellington Convention Centre.⁶¹
103. Finally, while not directly raised in the Statement of Issues, there are also numerous examples of resellers supplying to projects in areas where the reseller does not have a warehouse, showroom, or local sales force. The parties will provide a list of those examples separately.

E. No vertical effects

104. The parties reiterate their view that there is no basis to believe that the acquisition will result in vertical effects.
105. For the reasons explained at [70] to [76] above, the parties agree with the Commission that manufacturers would not have an incentive to allow vertical effects to arise.⁶² This is

⁵⁹ Statement of Issues, at [105].

⁶⁰ Statement of Issues, at [103].

⁶¹ The parties will provide a more comprehensive list of examples separately.

⁶² Statement of Issues at [9]-[10].

consistent with what manufacturers have told the Commission,⁶³ and the Euroquip/Moretti Forni example described above. Simply put, and with all due respect to the Commission, if there was any chance that the merged firm could become an indispensable distribution channel, Moretti Forni would not have taken the action it did.

106. This should be sufficient evidence for the Commission to be satisfied that vertical effects are unlikely.
107. The parties also reiterate the point made in [105]-[108] of the Clearance Application that the Commission would be committing an error of law if the Commission declined clearance based on a concern that the merged firm might enter into an anti-competitive agreement (exclusive or otherwise) with another unknown party at some unknown point in the future.
108. If the merged firm entered an anti-competitive arrangement in the future, then that is a separate and distinct matter for the Commission to consider on its merits under Part 2 of the Commerce Act. The Commission cannot decline clearance on the basis that the merged firm might do something else that is unlawful in the future.

⁶³

For example, Statement of Issues at [113].