

**Foodstuffs Statement of Issues Response on Substantially Lessening of
Competition in the New Zealand Supermarket Industry**

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Public Version

Executive Summary:

The Foodstuffs merger should not be approved. The evidence of abuse of market power is already present within market, which will increase barriers to entry for other retailers as suppliers will fear retaliation if they partner with new entrants. The market study acknowledged more competition is needed, so to approve a merger to reduce competition so soon after or at all, would render the work and efforts of the last three years redundant.

1. Introduction

It appears based on the statement of issues issued by ComCom, that there are a high number of concerns raised about the merger and its impact on competition. The merger will increase barriers to entry for new entrants into this market, based on the stronghold this mega retailer would have. This in effect will keep prices high in New Zealand, or make them higher, and continue to drive food manufacturing out of the nation due to increasing margin requirements to improve profits for its shareholders.

2. Substantially Lessening of Competition – Framework of Assessment

As was submitted in my first submission to ComCom, New Zealand is already the most concentrated grocery retailing market in the world prior to the merger across 3 different measures of concentration HHI, C4 and population per supermarket¹. The 2022 market study final report noted the need for more competition in market. If the merger is to go ahead it will not only lessen competition in the current market, but also increase barriers to entry for future competitors. The barriers to entry include the power held over suppliers to not supply new entrants at the risk of losing business with Foodstuffs. This conduct can be seen already with The Warehouse Group's attempt to offer lower prices on Weetbix², of which it suddenly lost supply. Although this example has been remedied as it was taken to the media, it demonstrates challenges for even established businesses to extend their grocery offer due to the lopsided bargaining power that sits with the current retailers, in their current capacity of 3 retailers, as opposed to 2.a

The stated rationale by the parties of the Proposed merger is to “create a world-class, customer-driven national food and grocery retailer and wholesaler”. There should be nothing stopping either business from becoming national companies in their own right and entering competition in the island which they do not currently compete. This assumes there is no agreement to not enter each other's territories which could be considered a condition of cartel conduct if it does exist.

3. The Increase in Buyer Power – Risk to Loss of Food Sovereignty

As has been discussed already, the merged entity would create an increase in buyer power if it were to go ahead. The consequence of this will result in further lopsided negotiations, as the buyers in the market go from 3 to 2. The only party which would benefit from this concentration of power is Foodstuffs, at the expense of its customers and suppliers. This increased buyer power also puts New Zealand at further risk of losing more manufacturing to offshore. The latest announcement of Sanitarium closing down cereal lines within its Auckland factory, is deeply concerning for NZ manufacturing³. The importance of food sovereignty, and NZ being able to produce the food it needs and not rely on imports should not be overlooked. As was seen through major world events such

¹ https://comcom.govt.nz/_data/assets/pdf_file/0025/343735/FSNI-and-FSSI-merger-Lisa-Asher-submission-in-response-to-Statement-of-Preliminary-Issues-9-February-2024.pdf

² <https://www.newshub.co.nz/home/money/2023/10/sanitarium-backtracks-on-decision-to-cut-off-the-warehouse-s-weet-bix-supply.html>

³ <https://www.thepost.co.nz/business/350228464/sanitarium-axes-49-jobs-drops-many-cereal-lines>

as Covid and climate change, producing food locally has become so much more important. The merger cares for profits, not for local manufacturing.

The prioritization of profit by Foodstuffs over supporting local producers was evident in the Sealord negotiations in November 2021⁴. Sealord according to media offered 50% gross margin to Foodstuffs for its NZ caught fish, but this fell short of Foodstuffs expectations, and they instead supported foreign imports over locally sourced. The food production and regulation standards of China and Vietnam are not the same as NZ, nor the same workforce protections. A margin request of 50% is extremely high, especially for a frozen product which has 12-24 months shelf life. This is significantly more than the US, which due to the higher nature of competition would not have a margin request beyond 30%, and realistically much lower than this. Although some of Sealord's range has been brought back in a limited capacity, significant damage to this business and its employees has been done. This example illustrates the power the retailer has, how it will enforce its power if it does not receive the margins it demands. This consequently will impact the shopper through higher prices, and impact NZ businesses with the reduction in local business and competition as the margin levels required will continue to increase.

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⁴ <https://newsroom.co.nz/2021/10/10/foodstuffs-deletes-nz-seafood-brands-to-make-way-for-more-imports/>

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4. Merger Does Not Equal Expansion

The submission by Anonymous E⁵ in arguing that the merger will create more stores in the South Island is ill conceived. There is nothing stopping Foodstuffs South Island from opening more stores in the South Island without the merger. As was noted in my prior submission, there are 4x more people per store in New Zealand than there is in Germany, and 3x more than other developed nations. This therefore means the traffic and spend

⁵ https://comcom.govt.nz/_data/assets/pdf_file/0027/349902/FSNI-and-FSSI-Anonymous-submission-in-response-to-Statement-of-Issues-7-April-2024.pdf

per site in New Zealand generates significantly more revenue and return per site than other countries. The additional proposition of the better instore experience of Foodstuffs stores versus those of WWNZ should perhaps be looked through the lens of profitability. Foodstuffs financial statements do not demonstrate the full value chain to shoppers, but only those of its centralized distribution and head office. Store revenue and profitability is not reported, unlike WWNZ. Therefore, perhaps given the investment in stores and the increase in store owner operator wealth as per the NBR rich list⁶, it could be argued that these stores are generating more profit and wealth to the detriment of its shoppers and community, and the investment in stores is a byproduct of their profitability at the expense of shoppers.

5. Monopsony Power

It was argued by Houston Kemp of the distinction of using a monopsony power framework versus a bargaining power framework is appropriate⁷. There was a lengthy submission on arguing this from an economic perspective, which lacked a commercial understanding. As there are 3 supermarket buyers present in New Zealand for groceries, there is no case for one buyer for a supplier. Suppliers currently have 3 major options locally to sell their produce, and other smaller alternatives within retail, and also foodservice wholesale.

“b. unless the buyer has substantial power in its downstream market, it will have no incentive to reduce the quantities it purchases in the upstream market, because it is likely to be more profitable for the firm to pass through at least some of any lowering of input prices into the downstream market and so compete more intensively in that market.”⁸

As per the statement above, the retailers already have significant power in the downstream market, particularly when it comes to produce. It is much harder for growers of produce to tightly manage production of these items, as they are impacted by weather and other inputs. Due the vulnerability of growers at the bargaining table, which has been illustrated at length in Australia recently with the Senate Inquiry on price gouging. Growers are more often price takers, which is resulting in lack of viability and exiting of growers from the industry⁹. Australia is also a highly concentrated market like NZ, with a large surplus of produce wasted, rather than sold by retailers at lower prices¹⁰.

“Our biggest customer is the rubbish bin,” one vegetable grower recently told the ABC.

⁶ <https://www.nbr.co.nz/business/nbr-rich-list-how-grocery-barons-rise-to-the-top/>

⁷ https://comcom.govt.nz/_data/assets/pdf_file/0023/346181/Houston-Kemp-Economic-effects-of-the-proposed-merger-of-Foodstuffs-North-Island-and-Foodstuffs-South-Island-7-March-2024.pdf

⁸ https://comcom.govt.nz/_data/assets/pdf_file/0023/346181/Houston-Kemp-Economic-effects-of-the-proposed-merger-of-Foodstuffs-North-Island-and-Foodstuffs-South-Island-7-March-2024.pdf

⁹ <https://nff.org.au/media-release/exploitive-powers-of-supermarkets-confirmed-with-growers-forced-to-foot-the-bill-while-bunnings-gets-a-free-pass/>

¹⁰ <https://www.abc.net.au/news/2024-03-13/does-a-supermarket-duopoly-mean-more-food-waste/103559734>

They said they didn't want to be identified for fear of retribution from Coles and Woolworths.

"The supermarket lawyers scare us all," they said.

Peak grower group AUSVEG said "the situation is so dire" that 34 per cent of growers were "considering walking away from their farming businesses".¹¹

What is quite striking about this, is the fact that many shoppers now face challenges in affording everyday essentials, and although there is no monopsony power present, the imbalance of bargaining power between grocery retailer and grower is evident at the bargaining table. A high amount of produce is dumped instead of sold at a lower price to benefit shoppers through this cost-of-living crisis, as it will dilute the retailers profit margin at a lower sell price.

6. Proposed Remedies and Australia Competition Law Reform

Although ComCom has made it known through its SOI that it does not have divestiture powers to review prior mergers and the lessening of competition, it is recommended that they recommend to government to consider empowering ComCom with these powers. As it is currently being reviewed in Australia¹² through the amendment of the competition and commerce act, of which NZ should also follow. The annual address in the Bannerman Competition Lecture¹³ held this month in Australia announced by Treasurer Jim Chalmers that major reforms are coming for Australian competition law. It was acknowledged that competition has been declining since the 2000's with market concentration across industries. The changes are intended to positively impact competition to provide more choice, better quality, and cheaper prices. The declining productivity was also noted as a concern to address through these reforms. New Zealand and the ComCom should take note of these developments, as its situation and circumstances are also similar. Currently in Australia mergers have a voluntary mandate to notify the ACCC, and this will be changed to mandatory, with the ability to review the last 3 years of mergers.

"Chalmers says Australia's merger laws are "no longer fit for purpose" because the ACCC "isn't properly equipped to detect and act against anti-competitive mergers"¹⁴.

It is strongly recommended that New Zealand undertake a similar review, as the concentration of industries in New Zealand with particular attention to the grocery

¹¹ <https://www.abc.net.au/news/2024-03-13/does-a-supermarket-duopoly-mean-more-food-waste/103559734>

¹²

[https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Supermarket_Prices/DivestiturePowersBill2024#:~:text=The%20Competition%20and%20Consumer%20Amendment%20\(Divestiture%20Powers\)%20Bill%202024%20seeks,section%2046%20of%20the%20Act.](https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Supermarket_Prices/DivestiturePowersBill2024#:~:text=The%20Competition%20and%20Consumer%20Amendment%20(Divestiture%20Powers)%20Bill%202024%20seeks,section%2046%20of%20the%20Act.)

¹³ <https://www.accc.gov.au/about-us/conferences-and-events/bannerman-competition-lecture/bannerman-competition-lecture-2024>

¹⁴ <https://www.theguardian.com/australia-news/2024/apr/10/labor-government-australia-competition-laws-mergers-jim-chalmers>

industry, is more concentrated than Australia, and therefore necessary to reform. Although the responsibility of this does not sit with ComCom, it is recommended that ComCom make this this recommendation to help improve the competitive landscape in New Zealand.

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7. Conclusion

It is strongly recommended that ComCom oppose the merger of FSNI and FSSI, as it will increase bargaining power of this mega-retailer to a market share of 60%. New Zealand is already the most concentrated grocery market in the world, with some of the highest prices in the world. It would be to the detriment of the nation if this merger were allowed to proceed, as it will increase barriers to entry with more market power, and exploitation further of bargaining power with its suppliers and customers. It will then continue to reduce competition within its stores through the coordination of conduct currently executed by FSNI within its categories as it tenders placement on shelves to the South Island. The ability to then charge higher prices again becomes possible, as competition continues to be removed.