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Sam Holmes and Susan Brown
Competition Branch
Commerce Commission
PO Box 2351
WELLINGTON 6140

By email:
registrar@comcom.govt.nz
sam.holmes@comcom.govt.nz
susan.brown@comcom.govt.nz

Tēnā kōrua Sam and Susan

Statement of Issues: proposed Foodstuffs merger

We thank you for the opportunity to comment on the *Foodstuffs North Island and Foodstuffs South Island: Statement of Issues (SOI).*

Attached is our submission which includes further analysis from our supplier survey data in response to the SOI.

We wish to reiterate our availability to meet in person to discuss further.

Ngā mihi nui

Raewyn Bleakley

Chief Executive

Commerce Commission

Statement of Issues

Notice seeking clearance for the proposed merger of Foodstuffs North Island Limited and Foodstuffs South Island Limited

Submission by the New Zealand Food and Grocery Council

26 April 2024

NZFGC SUBMISSION ON SOI FOR FS MERGER CLEARANCE APPLICATION

Contents

1. ABOUT THE SUBMITTER

1.1 The New Zealand Food and Grocery Council (**NZFGC**) welcomes the opportunity to comment on the Commerce Commission's (**Commission's**) Statement of Issues (**SOI**) dated 4 April 2024 and the underlying Notice seeking clearance for the merger of Foodstuffs North Island Limited (**FSNI**) and Foodstuffs South Island Limited (**FSSI**) (the **Application**)[1]. We refer to the two Foodstuff entities collectively as "Foodstuffs" (**FS**) where appropriate.

1.2 NZFGC represents the major manufacturers and suppliers of food, beverage, and grocery products in New Zealand. This sector generates over $40 billion in the New Zealand domestic retail food, beverage, and grocery products market, and over $34 billion in export revenue from exports to 195 countries – representing 65% of total good and services exports. Food and beverage manufacturing is the largest manufacturing sector in New Zealand, representing 45% of total manufacturing income. Our members directly or indirectly employ more than 493,000 people, one in five of the workforce.

2. INTRODUCTION

2.1 **Overview:** NZFGC thanks the Commission for this opportunity to submit on the Statement of Issues (**SOI**).[2] We consider that the Commission correctly reached the preliminary view it *cannot be satisfied* that the proposal is not likely to substantially lessen competition (**SLC**) in relevant markets. We also consider that must be the final determination.

a. It is *self-evident the proposal would likely SLC in relevant markets* given the enhanced buyer-power (fewer options) and increased barriers to entry and/or expansion (plus removing potential for more competitive counterfactuals), given:

i. the findings in the Market Study into the retail grocery sector (**Market Study**);[3] and

ii. that this is a 3:2 merger in an industry with vertical integration, high barriers to entry and expansion, and limited competition.

b. We submit there is *no basis on which the Commission could reach the requisite level of satisfaction* there would not likely be an SLC and the Commission must confirm its preliminary views. While the Commission naturally seeks evidence on various points, much is unlikely to be forthcoming (including due to fear of potential 'retaliation') and the onus remains on the applicants to demonstrate no likely SLC.

c. We further submit that the *issues are even more clearly identified taking:*

i. a proper approach to all likely counterfactuals (rather than assuming the (stated) status quo benchmark) and

ii. a broader whole of supply chain approach to the analysis.

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[1] FSNI-FSSI-clearance-application-14-December-2023.pdf (comcom.govt.nz)
[2] https://comcom.govt.nz/__data/assets/pdf_file/0037/348859/FSNI-and-FSSI-Statement-of-Issues-4-April-2024.pdf
[3] Market-Study-into-the-retail-grocery-sector-Final-report-8-March-2022.pdf (comcom.govt.nz)

2.2 We **agree** with the approach taken in the SOI and the concerns identified by the Commission. In particular:

a. **We agree with the concerns that the proposal would SLC / increase market power in the market for the *acquisition of groceries***:

i. It would be a reduction in the number of options for suppliers from 3 to 2, compared to the status quo.

ii. It would likely result in unilateral and coordinated effects in this market.[4]

b. **We agree with the concerns that the proposal would likely SLC / increase market power in the market for the *retail supply of groceries:***

i. It would increase buyer power impacting rivals' ability to acquire groceries on competitive terms with the merged entity.[5]

ii. It would lead to a large, combined set of data on sales and customer insights that would overwhelmingly disadvantage smaller rival retailers in insights for retail strategy.[6]

iii. It would increase barriers to entry and/or expansion in relation to the *Retail supply of groceries*.

iv. It would further enable strategic barriers.[7]

c. **We agree it is *necessary to look more broadly*, considering commercial dependencies between markets, and the fact that *each of the 3 RGRs operates an essential "platform"*[8] with the consequent self-preferencing and related concerns (notably on private label).**

2.3 We have the following concerns about the approach taken in the SOI:

a. **We have *concerns* as to the basis for the Commission's conclusion that the *wholesale supply of groceries "is not currently a focus"*:**[9]

i. We can only see two paragraphs in the SOI which deal with this aspect. Furthermore, the issue is dismissed.[10] Further expansion of the basis for this is necessary if we are to make submissions that would assist the Commission.

ii. As noted in our earlier submission, merging 2 of 3 RGRs could frustrate parliament's legislative intent, given that FSNI and FSSI are separately listed

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[4] We agree with the Commission on the different ways the reduction in competition would emerge at 62.1 of the SOI; that there will be buyer power (paragraph 47); and with the submissions noted in footnote 42 of the SOI.
[5] Paragraph 55.1 SOI.
[6] Paragraph 55.2 SOI.
[7] Paragraph 55.3 SOI.
[8] We agree with paragraph 25 SOI: *"..that there are important commercial dependencies between markets that are relevant to our assessment but are **not covered in the above discussion** of acquisition and selling markets. **Supermarkets are two-sided markets (platforms)** because there are indirect network externalities, and the volume of trade depends on price structures. For example, market power in acquisition markets likely derives from scale or market share in selling markets."* [emphasis added]
[9] Paragraph 60 SOI.
[10] Paragraphs 59 and 60 SOI.

as regulated grocery retailers in section 8 of the Grocery Industry Competition Act 2023.

b. **We are concerned the approach to the counterfactual taken to date in the SOI is incorrect and may potentially minimise the anticompetitive effects:**

i. The counterfactual is not necessarily the status quo. The SOI may at times indicate subconscious bias by consistently comparing the proposal to the (stated) status quo. This is further compounded by the reference to a confidential counterfactual attachment to the SOI.[11]

ii. In order to objectively assess the counterfactual, the Commission needs to consider the internal mechanisms (Co-op exit barriers) and why the parties do not compete.

iii. If the Commission chooses to not to consider these issues, then there is no basis on which it can be "*satisfied*" that there is no SLC, given there could be cartel provisions and/or the arrangements within and between the two FS entities may themselves be anti-competitive.

iv. The comment in the SOI that only a court can reach these views, while strictly correct, is inconsistent with the Commission's role to investigate and enforce potential breaches of the Commerce Act. The Commission is *required* *"to be an impartial promoter and enforcer of the law"*.[12]

v. The applicants should not be able to benefit from a potential cartel provision and/or rely on it to demonstrate that there is no SLC. The current arrangement where there is sharing markets raises concerns of cartel-like behaviour.[13]

vi. These are not new issue. We raised these issues in the Market Study. Nor are we the only ones to raise these concerns..

c. **We are concerned that an analysis of the effect on cooperative arrangements is missing.**

i. The SOI recognises that the Parties are separate legal entities,[14] but it does not include an analysis of how the two co-operatives operate, individually and together, and how that will change because of the proposal.

ii. Co-operative structures can include barriers to exit, which can have a substantial impact on competition in the relevant markets. Prudent co-operatives establish structures which reduce these exit barriers. We would be happy to submit further on this point as the Commission does not seem to have considered these issues to date.

[11] Paragraph 54 SOI.
[12] https://comcom.govt.nz/about-us/our-role
[13] NZ-Food-and-Grocery-Council-Submission-on-Market-study-into-grocery-sector-draft-report-26-August-2021.pdf paras 1.15, 7.6 7.47, 7.13e and 7.66d; see also paragraph 7.47 which reads: *"NZFGC also recommends the Commission investigates whether agreements between Foodstuffs North Island and Foodstuffs South Island are illegal cartel arrangements."*
[14] Paragraph 13 SOI.

iii. The separate co-operatives may behave in differently towards members, and there is no discussion about whether individual stores in each co-operative may have less countervailing power against a bigger "head office" as a result of the proposal.

2.4 **We reinforce that the evidential burden and onus is on the applicants and that *"A lessening of competition is generally the same as an increase in market power"***:[15]

a. The **onus** is on the applicants to satisfy the Commission. Naturally the Commission seeks further information from suppliers. However, as the Commission knows, the concentrated nature of the industry, ease of identification and the concerns of retaliation mean that such evidence may not be likely to be forthcoming.

b. The Commission cannot and must not consider the **absence of evidence in relation to these issues to be evidence that they do not exist**. Quite the reverse, considering the Market Study clearly identified these concerns.

c. We reiterate that the s 47 Commerce Act test must be applied consistently with the precedent set in the Court of Appeal in *NZ Bus and Infratil v Commerce Commission* [16] that competitive impact may be "*minor*" but can nonetheless constitute a substantial lessening of competition.[17]

2.5 **We also submit that the Commission must consider the relevance of Australian developments particularly the current *Select Committee on Supermarket Prices*.**[18] It is instructive that Professor Allan Fels, prior ACCC chair and currently honorary professor at both Melbourne and Monash Universities, has made the following observations:

a. **The importance of market structure:** (relevant here given the intention to have further concentration: "My own thinking on this, such as it is, originates from very elementary economics. If you study monopoly and market power dominance, it is always associated with a very high degree of concentration in a market—very high market shares. There may be some other factors, like entry barriers et cetera, but, essentially, it is a structure of concentration that creates a capacity to do harm to consumers and to other businesses. On occasion, the right answer is to break up the firm."

b. **The need for a longer term perspective on the impacts of permanent structural change:** (particularly when we are concerned about a merger which would not only "paper over" potentially anti-competitive / cartel arrangements but also permanently prevent more competitive counterfactual from emerging, i.e. a "loss of options"): "Competition law has a really big long-term effect on competition. The payoff long-term to consumers is very large. The short-term effect is not necessarily terribly big. The short-term effect of breaking up a cartel sometimes can be considerable. But

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[15] Paragraph 6 of the Commission's **MAG**: https://comcom.govt.nz/__data/assets/pdf_file/0020/91019/Mergers-and-acquisitions-Guidelines-May-2022.pdf

[16] *New Zealand Bus Limited and Infratil Limited v Commerce Commission* [2007] NZCA 502 Wilson J at [270]: *"More particularly, pre-acquisition competition between NZ Bus and Mana in tendering for a small number of routes is of itself sufficient to establish that substantial (in the sense of real) lessening of competition would result"*. At [272] *"On the present facts, only very minor lessening of competition would result, and the consequent detriment would be modest."*

[17] This has been recognised in the SOI at paragraph 23/footnote 18.

[18] ParlInfo - Select Committee on Supermarket Prices : 15/04/2024 (aph.gov.au)

merger decisions and abuse of dominance decisions typically have a significant effect but not an overnight effect."

c. **The Commission's responsibility to prevent adverse structural change**: "In the eighties, if the ACCC had blocked Woolworths Safeway, I think we would have had a much more competitive retail sector."

2.6 These observations are consistent with the Court of Appeal's determination the competitive impact may be minor but still constitute an SLC.

2.7 In addition, we note:

a. This is one of the most significant and complex mergers to be assessed by the Commission, given the background of the Market study.

b. However, parties have been given only a very limited time to provide submissions on the SOI. We do not feel like we have been able to provide as detailed or meaningful a submission as we would like in the time available.

c. There is a significant amount of confidential information, including a confidential submission on the counterfactual, which makes it difficult for parties to provide submissions and means that the information provided by the applicants is not being adequately or properly tested.

2.8 **The proposal is uniquely straightforward with no "upside" and considerable "downside" and must be declined**: There are clear risks to competition and consumers, yet no indication that this is necessary to compete or evidence that consumers would benefit. In short, there is only potential downside for consumers (and suppliers) and the risks are real.

2.9 **The Market Study identified concerns about the concentration in the grocery sector and measures to de-concentrate the industry were considered by the government. It would seem surprising to allow a proposal that would result in further concentration and exacerbate known issues.**

3. CONTEXT, MARKET STRUCTURE AND IMPACT OF THE PROPOSAL

3.1 **Overview:** It is important to consider the impact of the proposal in the context of the market structure. Market structure matters, as it drives conduct and performance.

3.2 **Market Study findings:** The Commission's main findings in the Market Study were:

a. a (retail) market duopoly;

b. the intensity of competition between the major grocery retailers was muted and did not reflect workable competition;

c. entry and/or expansion by other grocery retailers was difficult;

d. the retailers' profitability appeared higher than expected under workable competition;

e. prices appeared high by international standards;

f. levels of innovation appeared low;

g. pricing, promotions, and loyalty practices limited consumers' ability to make informed decisions; and

h. competition was not working well for many suppliers due to an imbalance in market power.

No evidence has been provided to indicate that the above have demonstrably improved since the Market Study. In fact, one retailer (Supie) has exited the market, and others exiting earlier (Honest Grocer).

3.3 **Other potential distortions not investigated:** The Commission did not investigate if:

a. The FS intragroup arrangements (e.g. holding land ownership at head office level) created artificial barriers to exit/switch (by individual store owners) and therefore substantially lessened competition.

b. If there were potential cartel provisions and/or SLC issues between the FS entities (despite this being raised in submissions).

3.4 **Contrast with past inquiries and our submissions:**

a. This can be contrasted with the approach taken in the earlier fuel sector inquiry, which led to Commission recommendations and legislative changes enabling tied resellers to switch banners more easily.[19]

[19] **Market study into the retail fuel sector- Final report – Executive summary:** Para x108: *"We have made recommendations to limit the use of certain terms in wholesale supply contracts to give resellers' more freedom to obtain competitive supply arrangements."*; see also s17 Fuel Industry Act 2020 (Right to terminate certain fixed wholesale contracts)

b. We had raised the concerns noted in paragraph 2.3 above in our submission to the Commission in response to its draft Market Study report.[20]

3.5 **Market dynamics:** We submit that the Commission should also consider current market developments which may make market entry less likely and/or otherwise adversely impact competition / consumers. We note here:

a. Countdown's rebranding to Woolworths seems consistent with increased private label, which may also mean increased offshoring of supply and increased pressure on suppliers.

b. Currently we are aware that FSNI is undertaking category reviews in which has been reported to us from suppliers that the stated aim is often a reduction in SKUs.

c. The Grocery Supply Code was introduced to help address bad behaviour of the RGRs towards suppliers and help with the allocation of risks to the party best placed to manage them.[21] However, there have been a number of concerns raised by the Grocery Commissioner about the grocery supply agreements offered by FSNI and FSSI to suppliers.[22]

d. Given this is a live issue, and is challenging to assess given changing day by day, at the time of writing we remain concerned that the approach taken by FSNI and FSSI to contract out of the key protections of the Grocery Supply Code in their separate (and substantially different) template agreements is in breach of the RGRs' obligations to act in good faith, and to contract out only where it is reasonable circumstances taking into account the benefit to suppliers.

3.6 **The proposal would materially impact intra-group arrangements; the FS head office would have greater bargaining power relative to individual co-operative members and greater centralisation (rationalisation) can be expected:** While this may lead to efficiencies and / or cost-savings, it seems likely to:

a. reduce the prospects of new supply (as suppliers, especially local ones, tend to start small with a 'toehold' or niche);

b. reduce innovation; and

c. lessen consumer choice.

[20] NZ-Food-and-Grocery-Council-Submission-on-Market-study-into-grocery-sector-draft-report-26-August-2021.pdf paras 1.15, 7.6 7.47, 7.13e and 7.66d; see also paragraph 7.47 which reads: *"NZFGC also recommends the Commission investigates whether agreements between Foodstuffs North Island and Foodstuffs South Island are illegal cartel arrangements."*

[21] Market Study report, 8.102-8.104.

[22] Open letter to grocery sector dated 16 April 2024. (https://comcom.govt.nz/__data/assets/pdf_file/0033/349791/Commerce-Commission-Open-letter-to-the-grocery-sector-Focus-of-the-grocery-regulator-2024-16-April-2024.pdf) and Correspondence between the Commission and RGRs released on 16 April 2024 (https://comcom.govt.nz/__data/assets/pdf_file/0032/349592/Commerce-Commission-letter-to-Foodstuffs-North-Island-on-grocery-supply-agreements-9-February-2024.pdf and https://comcom.govt.nz/__data/assets/pdf_file/0033/349593/Commerce-Commission-letter-to-Foodstuffs-South-Island-on-grocery-supply-agreements-28-February-2024.pdf)

4. SUBSTANTIALLY LESSENING OF COMPETITION / INCREASED SUBSTANTIAL MARKET POWER IN THE ACQUISITION OF GROCERIES

4.1 **We agree with the concerns that the proposal would SLC / increase market power in the *Acquisition of groceries*:**

a. We agree that, compared to the status quo, it would be a reduction in the number of options for suppliers from 3 to 2.

b. We agree this would likely result in unilateral and coordinated effects in this market.[23]

4.2 **We agree with the Commission's "main concerns":**

> *"[relating] to the potential for the merged entity's buyer power to result in unilateral and coordinated effects in upstream market(s) for the acquisition of groceries."*
> ...

and that this is:

> ...
> *" ... one of the ways in which competition in downstream retail grocery markets could be impacted by the Proposed Merger."*[24]

4.3 **The current Australian Select Committee on Supermarket Prices** has seen the Senate also focus on size and whether it matters for Suppliers. In reality, even the largest supplier has little 'leverage' over the retailers. Assuming (taking a conservative position) that the sector's value is as low as $18.1B (noting the Commission has higher figures), even a large supplier with say $750MM of turnover or 4% has little power especially against a merged FS.

4.4 **We consider that these issues are self-evident, given the reduced options and likely greater centralisation of procurement (with less ability and incentives for local stores to depart from "head office" directives).** We also urge the Commission to consider past conduct, present initiatives, and the fact the proposal will mean an enhanced ability to engage in strategic conduct.

4.5 **We note that the Commission is continuing to investigate:** the extent to which the Merged Entity (**ME**) compared to FSSI and FSNI:

a. may be able to:

i. ***"negotiate lower prices it pays for goods from suppliers and/or otherwise obtain terms of supply more favourable"****; or*

ii. *"give the merged entity greater ability and incentive to increase the* ***penetration of private label products*** *(potentially resulting in some suppliers of branded grocery products getting squeezed out and less choice/range for consumers)"*

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[23] We agree with the Commission on the different ways the reduction in competition would emerge at 62.1 of the SOI; that there will be buyer power at 47 of the SOI; and with the submissions noted in footnote 42 of the SOI.
[24] Paragraph 45 SOI.

b. *"may result in **fewer opportunities for new or innovative suppliers or products to be sold by the major grocery retailers, slowing the pace of product innovation** (and ultimately reducing the range and quality of grocery products available)"*

4.6 **Taking these points in turn:**

a. We submit:

i. The application is predicated on costs savings and efficiencies. Some of these will necessarily come from the ME's increased buyer power and ability to negotiate with suppliers.

ii. The ME would clearly have the ability and incentives to expand private label, especially when the only competitor seems to be adopting that path (coordinated effects).

iii. Further, this allows the RGRs to obtain a further monopoly in relation to that data and for media services in respect of which they can charge monopoly rents (utilising their own vendors). They leverage their market power to effectively bundle those "services" for many suppliers, as they can be essential inputs (and key factors in commercial and commercial negotiations). The above will obviously have those adverse effects especially with greater centralisation (and a reduced level of individually owned store control due to the greater power imbalance).

4.7 Given the findings of the Market Study, and that regulation was required to address the anti-competitive effects in the market and provide some protections for suppliers, we cannot see how the Commission can be satisfied that the proposal will not SLC. The Grocery Industry Competition Act 2023 and the Grocery Supply Code have only just come into effect, and it is not yet clear to what impact this will have. Further consolidation of RGRs will only increase buyer power.

4.8 As noted above, the approach taken by the Parties to the grocery supply agreements and compliance with the Grocery Supply Code indicate that a significant imbalance of power remains between the RGRs and suppliers. We remain concerned and of the view that the new regulatory regime is in a very early stage and will take further time and effort by a number of parties to have the desired effect intended. We note that in the recently published correspondence published between the Commission and FSNI and FSSI, that the initial grocery supply agreements offered raised potential compliance concerns, and a number of areas were identified with both FSNI and FSSI were urged to consider the feedback immediately and to make changes to meet the requirements of the code in a way that best promotes the purpose of the code.

4.9 Further consolidation will only exacerbate these issues and result in more concentrated power for the ME.

4.10 **We submit it is the applicants who must demonstrate that these harms will not occur**.

4.11 **We note Houston Kemp's (HK) submission on the bargaining model**. While this is not our area of expertise we note that these theoretical models are helpful but can be divorced from the real world and reliant on assumptions (including rationality).

4.12 **We also note the ACCC's comments in the report that HK refers to, and the ACCC's acknowledgement of "complications" with the model:**[25]

"The general result is that the strong outside options for a buyer, or weak outside options for a seller, are a major source of buyer power in a bilateral bargaining framework."

"Bilateral bargaining typically does not occur in isolation. Even though retail supply contracts are typically bilateral, large retailers often negotiate simultaneously with a large number of suppliers, and suppliers negotiate with more than one retailer.

4.13 **The ACCC discusses (at 14.4.1) the "*Absolute size of the buyer*" and (at 14.4.2) the *"Relative dependency of the relationship"* which is critical in NZ (and which would be fundamentally impacted by removing the dependency from three parties to two)** [emphasis added]**:**

*A second possible, and potentially important, source of buyer power raised in the economic literature is the r**elative dependency of two parties on a particular buyer–seller relationship.** The idea is that, where a buyer and a seller are in a supply bilateral relationship and the **relationship is of substantial financial importance to the seller but of lesser importance to the buyer, this will impart bargaining power on the buyer**.*

4.14 **The ACCC also commented (at 14.4.3) on Private Labels:**[26]

If the buyer has its own private labels that compete with the seller's product (or if the buyer can readily create and have manufactured such private label goods), then this is likely to be a further source of buyer power.

... The ACCC notes that there is some empirical economic evidence that private label goods do in general bestow greater bargaining power on retailers.

4.15 The above indicates that in the NZ scenario the proposal will increase "buyer power", which in this context we submit necessarily equates to an increase in market power (which the Commission equates to a lessening in competition).

4.16 We note the Commission is also considering *"the extent to which a substantial lessening of competition may occur whether or not there is a reduction in volume or output"*.[27] That consideration should be swift and answered in the affirmative – clearly there can be a reduction in quality and innovation which are key components of competition.

4.17 Should that not be the Commission's response, we would request the opportunity to submit further on what seems to be a fairly obvious point and inconsistent with the Commission's own Guidelines which explicitly refer to non-price (and indeed non-quantity) *factors "such as **quality** or service below competitive levels"*[28], and ***"quality, range,** level of **innovation, service** or any other element of competition"*[29] [emphasis added].

[25] https://www.accc.gov.au/system/files/Grocery%20inquiry%20report%20-%20July%202008.pdf at p 312.
[26] https://www.accc.gov.au/system/files/Grocery%20inquiry%20report%20-%20July%202008.pdf at p 315.
[27] Paragraph 40 SOI.
[28] Paragraph 6, MAG, https://comcom.govt.nz/__data/assets/pdf_file/0020/91019/Mergers-and-acquisitions-Guidelines-May-2022.pdf
[29] Footnote 4, MAG, https://comcom.govt.nz/__data/assets/pdf_file/0020/91019/Mergers-and-acquisitions-Guidelines-May-2022.pdf

4.18 **We agree with the Commission's current view and its reasons for that view and submit this should not change:**

a. **We agree that** *"the merged entity may be able to* ***unilaterally extract more favourable terms*** *from suppliers than it would in the counterfactual because of an increase in its bargaining power relative to suppliers. This* ***may cause immediate harm to suppliers*** *regardless of whether the merged entity* ***purchases less product from them****. In addition, we are concerned that* ***harm may also arise if suppliers have less ability and incentive to invest and innovate over time because the subsequent imbalance of bargaining power*** *increases risk and reduces their profitability"*[30] [emphasis added]

b. **We also agree that this is because (as the evidence indicates):**

i. *"FSNI and FSSI* ***each present separate opportunities*** *for suppliers to negotiate listings, prices, other terms of trade and contract renewals. FSNI and FSSI thus form part of the 'outside option' available to suppliers in their dealings with each buyer individually... The value of those suppliers outside option* ***would consequently be reduced. In contrast, the merged entity would continue to have many suppliers*** *from whom it could acquire grocery products, with little to no change in its outside options;"*[31]

ii. *"FSNI and FSSI sometimes compete directly for volume..."*[32]

iii. *"... both invest in new product development...but present separate opportunities for new suppliers, or existing suppliers with new products..."*[33]

iv. other existing grocery retail competitors may [will] not be sufficient to materially constrain the merged entity[34]

v. benefits include a wealth transfer which has the above adverse effects but no countervailing consumer benefits.

4.19 **In summary**:

a. We agree that there will be enhanced buyer power and, consistent with the submissions referenced by the Commission,[35] this will increase vulnerability of supply (including quality, innovation, and diversity/choice).

b. Again, we regard the matters which the Commission states that it is *"continuing to investigate"*[36] to be self-evident in relation to the obvious/presumptive harms that will occur, and we are of the view that the Commission cannot be satisfied there are no concerns on these matters.

[30] Paragraph 81 SOI.
[31] Paragraph 82.1 SOI.
[32] Paragraph 82.2 SOI.
[33] Paragraph 82.3 SOI.
[34] Paragraph 82.34 SOI.
[35] Footnote 42 SOI (Anonymous B, Anonymous C, Lisa Asher, and NZFGC).
[36] Paragraph 48 SOI.

c. In particular:

i. Negotiating lower prices/less favourable terms.[37] We do not accept that there is generally a surplus to be transferred and consider this to be inconstant with the Market Study conclusions.

ii. The increase in ability and incentives to increase the penetration of private label products with the adverse impacts.[38]

iii. Similarly, we agree that the proposal would result in *"fewer opportunities for newer or innovative suppliers of products to be sold by the major gross retailers, slowing the pace of product innovation (and ultimately reducing the range and quality of grocery products available)"*.[39]

iv. While we have concerns about the use of the word "*coordinate*" between the two major retailers, we agree that both parties would have increased market power in procurement knowing that suppliers had fewer options, and that there would necessarily be less competitive tension given the greater similarity in cost structures with similar effects to explicit or tacit collusion.

4.20 **We therefore submit that (following the Commission's approach)[40] the proposal would likely SLC / increase market power by virtue of:**

a. a transfer of surplus from grocery suppliers to the merged entity;

b. a reduction in choice or quality of groceries for retail consumers;

c. exit by suppliers from the acquisition market;

d. a reduction in the number of channels for suppliers to reach retail consumers, or a reduction in the number of opportunities suppliers have to pitch new ideas or products; and/or

e. a reduction in grocery suppliers' ability and incentives to invest or innovate.

[37] Paragraph 48.1.1 SOI.
[38] Paragraph 48.1.2 SOI.
[39] Paragraph 48.2 SOI.
[40] Paragraph 39 SOI.

5. SUBSTANTIALLY LESSENING OF COMPETITION / INCREASED SUBSTANTIAL MARKET POWER IN THE RETAIL SUPPLY OF GROCERIES

5.1 **We agree with concerns the proposal would likely SLC / increase market power in the *Retail supply of groceries:***

a. It would increase buyer power impacting rivals' ability to acquire groceries.[41]

b. It would lead (among other things) to a large, combined set of data on sales and customer insights.[42]

c. We agree that this will increase barriers to entry and/or expansion in relation to the Retail supply of groceries.

5.2 **We agree with the Commission's reason for not being satisfied there would be no SLC - and submit that there would be an SLC - in downstream markets for the *Retail supply of groceries* (with both unilateral and coordinated effects):** We agree there would be:[43]

a. *"a loss of actual or potential competition at the retail level"* between the parties**;**

b. The proposal would increase *"barriers to entry and/or expansion by third parties in retail grocery markets"*;

c. The proposal would increase *"the likelihood, completeness and sustainability of coordination between the merged entity and Woolworths"*.

5.3 **We also note that a merged entity could engage in more national pricing:** This will make it easier for a major competitor to 'coordinate' pricing. The Market Study concluded competition is already weak, and this merger **could** serve to strengthen coordination effects, reduce competition, and lift retail prices.

5.4 We submit that the commercial dependencies between markets, the fact that the parties operate powerful platforms enhance with sophisticated data and private label all indicate pre-existing competition concerns, which would be exacerbated by the proposal with no compensating benefits.

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[41] Paragraph 55.1 SOI.
[42] Paragraph 55.2 SOI.
[43] Paragraphs 131.1 – 131.3 SOI.

6. COMMERCIAL DEPENDENCIES BETWEEN MARKETS, PLATFORMS and PRIVATE LABEL

6.1 **We agree that:**

> *..there are **important commercial dependencies between markets** that are relevant to our assessment but are **not covered in the above discussion of acquisition and selling markets**. Supermarkets **are two-sided markets (platforms) because there are indirect network externalities, and the volume of trade depends on price structures.** For example, market power in acquisition markets likely derives from scale or market share in selling markets.*[44]

6.2 **The market power of each platform and concerns about Private Labels (and self-preferencing) was something we submitted on in the Market Study and relevant to this discussion:** e.g. [45]

> *4.12 There are a number of conflicts of interest here:*
>
> *a **Conflict of interest 1 – Retailers get significant inside information from suppliers:** Parties do not normally supply competitors with volume, cost/price, and promotional information. Indeed, as of 8 April this year cartel conduct is now a criminal offence.*[46]
>
> *As far as we know there are no measures to protect that information being misused for anti-competitive purposes.*
>
> *b. **Conflict of interest 2 – Price relativities at retail**. Retailers may not want competing, strongly branded goods, to be priced below their private labels and in some cases will reject deals for higher quality product because the branded product would be cheaper for consumers than the retailer's private label. Private labels might then set a price floor and reduce price competition. Conversely if the private label goods were regarded as better quality, then the ACCC's comments about the then [1] applicable level of comfort it was able to reach would not seem relevant (as, putting aside the other distinctions, they appear to have been in relation to lower price point private labels).*
>
> *c. **Conflict of interest 3 – quantitative issues – Retailers become competitors for vital shelf space**. Not only could this impact the viability of suppliers, but consumers may also miss out on the variety and innovation, particularly as quantities of private label increase.*
>
> *d. **Conflict of interest 4 – there may also be concerns about use of know-how and/or intellectual property belonging to the supplier.** It may unknowingly or unwillingly be forced to effectively gift this information and intellectual property to the Retailer. Suppliers have reported this to the NZFGC over the years.*

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[44] SOI para 25: FSNI-and-FSSI-Statement-of-Issues-4-April-2024.pdf (comcom.govt.nz)

[45] NZFGC-Comments-on-submissions-on-preliminary-issues-paper-12-April-2021.pdf (comcom.govt.nz)

[46] We included footnotes **[32]** *The impact of private labels on the competitiveness of the European food supply chain – study carried out by LEI, Reference No ENTR/ 2009/031* (PDF) The impact of private labels in SME competitiveness of the European food supply chain (researchgate.net); **[33]** The impact of the rise in private label brands on supplier/retailer relationships 8296.pdf (impgroup.org) [34] See for example Dana Mattioli *Amazon Scooped Up Data From Its Own Sellers to Launch Competing Products (23 April 2020)* Amazon Workers Used Data From Third-Party Sellers to Launch Competing Products, Contrary to Company Policy: Report - TheStreet

> *4.13* ***Retailers have different incentives when they also compete on the supplier level.*** *First, Retailers receive sensitive commercial information from suppliers and have a conflicting interest to use this information to improve their own competing private label or even force suppliers to become their manufacturers (i.e., requiring the supplier to also manufacture the Retailers' home brands as a condition of supply). Second, private labels are typically understood as a low-cost option, as the Retailers' own submissions suggest."*[47]

6.3 We note that some market distortions (but certainly not all) may be partially addressed in theory under the new regime, but its efficacy is by no means demonstrated or assured. The Code alone is unproven and as noted above the new regulatory regime will take further time and effort by a number of parties to have the desired effect intended.

6.4 Regardless, the Code was never intended to stop "hard bargaining", it was intended to increase efficiency for both sides (risk allocation to correct parties, greater transparency). From our perspective, there is nothing in the Code to address the increase in market power from a 3:2 buy-side merger. (Noting this would undermine legislature's intended comparability of three RGRs.)

6.5 **In the Market Study we also noted growing agency concern about self-preferencing (concerns that are getting more, not less, attention subsequently): See for example:**

a. Then-proposed US initiatives, including the then-proposed Ending Monopolies Act.[48]

b. Noting comments by (now) FTC chair Lina Khan about structural options to address these types of issues.[49]

c. Please also see NZFGC's *Consultation conference Day 7 - Follow up*[50]

6.6 **Self-preferencing, in a market in which a party operates – and in which that same party also is also a competitor (as is the case with private label and sponsored brands) – is obviously of great concern internationally:** There are numerous other articles reinforcing these growing concerns, such as:

a. *Using Antitrust Law to Address the Market Power of Platform Monopolies*.[51]

b. *Self-Preferencing in Digital Markets*[52] which notes:

i. Germany revamping its competition rules at the beginning of 2021, banning 'Undertakings of Paramount Significance' in multi-sided markets from presenting their own offers more favourably than those of rivals, and pre-installing their own offers when providing access to supply and sales markets.

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[47] Footnote [35] commented:" *Retailers therefore have a conflicting interest to ensure competing products are priced higher than this implicit price floor. Third, suppliers compete for limited supermarket shelf space. Retailers have a conflicting interest to favour the placement of their own private label products. There may be related IP issues"*.

[48] A pithy summary is here: a. https://www.crowell.com/NewsEvents/AlertsNewsletters/all/House-Antitrust-Reform-Bills[1] Could-Restrict-How-the-Largest-Online-Platforms-Do-Business-and-Influence-Future[1]Enforcement-Trend

[49] https://columbialawreview.org/content/the-separation-of-platforms-and-commerce/

[50] Incorrectly described (as it was an NZFGC submission) at this link: Andrew-Matthews-Consultation-conference-Day-7-Follow-up-2-November-2021.pdf (comcom.govt.nz)

[51] Using Antitrust Law to Address the Market Power of Platform Monopolies - Center for American Progress JUL 28, 2020

[52] https://globalcompetitionreview.com/guide/digital-markets-guide/second-edition/article/self-preferencing-in-digital-markets

ii. The (then) US move to a regulatory regime where a Digital Markets Unit (DMU), which is part of the Competition Markets Authority (CMA), can designate certain undertakings as having 'Strategic Market Status'.

iii. The UE Digital Markets Act (DMA) prohibiting digital platforms designated as a 'gatekeeper' from ranking their own products and services more favourably than those of third parties.

iv. ***"Competition enforcement is increasingly focusing on self-preferencing"*** **–** the article goes on to discuss theories of harm, noting *"the competition authorities tended to focus their evidence collection efforts on the existence and significance of foreclosure*."

6.7 The Commission rightly identifies that a two-sided platform approach is appropriate here (also the need to review the end-to-end supply chain, we submit, requires closer scrutiny as part of the Commission's review).

6.8 **Economic Consultants Castalia highlighted these issues concluding:**[53]

Whether private labels enhance, or harm consumer outcomes depends on the specific market context.

Private labels can alter the balance of bargaining power between retailers and suppliers.
If a retailer introduces a private label that is a sufficiently close substitute for an existing named brand, then the retailer's bargaining power will increase if the named brand cannot easily switch to its supply to other retail channels. The private label gives the retailer an outside option which improves the retailer's negotiating position (and conversely harms the supplier's negotiating position).

In diffuse retail markets, private labels will generally enhance consumer outcomes.

In highly concentrated retail grocery markets such as in New Zealand, control over the retail channel to market provides retailers with strong buyer power, which is accentuated by private labels.
In a highly concentrated retail market, an individual retailer has control over a key channel to market, providing the retailer with strong buyer power. The Draft Report finds that the two largest retailer groups account for 80 to 90 percent of the retail grocery market in New Zealand. The high concentration in New Zealand means that many grocery suppliers must secure a supply arrangement with at least one of the two retailers to achieve scale to supply efficiently. ***As a result, retailers hold a strong imbalance of power in the retailer-supplier bargaining relationship.***

6.9 **This is consistent with the Commission's concerns in the SOI and the "*distortions*" in the bargaining model outlined by the ACCC, the proposal would of course exacerbate these competition concerns, through greater concentration of economic power and reduced "options" (among other factors).**

[53] CASTALIA: Private Labels, Buyer Power and Remedies in the NZ Grocery Sector -Prepared for the Food and Grocery Council August 2021

6.10 **The Australian experience concerns about the private label impact:** Even in a larger and less concentrated market (which is subject to further scrutiny at the moment including the **current *Select Committee on Supermarket Prices***), a paper comments that while in 2013 there may have been some benefits of private label:

However private label brand growth has a range of potential negative effects for the Australian food industry, such as discouraging the level of innovation as well as jeopardizing the livelihoods of many smaller, independent suppliers, their families, and the communities in which they operate.[54]

6.11 **The Commission was right to consider in the Market Study *that "some aspects could dampen competition between suppliers":*** [55]That said, we submit that the Market Study may not have fully appreciated the severity of those potential harms, nor have taken a sufficiently forward-looking approach perhaps due to the nature of the Market Study (but which we submit it must clearly do here, with its forward-looking analysis).

6.12 **The Commission rightly noted the incentives issues, which is a factor critical for this evaluation (and confirmed by the above) namely:** [56] [emphasis added]

- *Consumers may benefit from private label products through lower prices and greater choice. However, **retailers of private label products can face conflicting incentives** given they are both customers and competitors of branded suppliers.*

- *While private label products could increase consumer choice and lower prices in the short term, there is a **risk that growth of private labels could crowd out supplier-branded products. This could lead to a loss of consumer choice and higher prices over the longer term.***

- ***The risk of private label products adversely affecting outcomes for consumers is greater when retail competition is relatively weak.** For example, competition could be harmed by retailers giving their private label products preferential shelf space or using suppliers' intellectual property.*

6.13 **We also endorse the following from the Market Study:**[57]

8.67 Dobson and Chakraborty (2008) describe retailers' and suppliers' relative dependence on each other as follows:[1043]

...in terms of relative bargaining power, the **leading retailers may find it straightforward and inexpensive to switch suppliers** (especially for commodity/ private-label goods, but more generally where shelf space can be reallocated across product categories without losing significant custom), and thus switching costs in these circumstances may be expected to be relatively low as long as alternative suppliers exist with sufficient capacity. **In contrast,**

[54] *The impact of the rise in private label brands on supplier retailer relationships* https://www.impgroup.org/uploads/papers/8296.pdf
[55] https://comcom.govt.nz/__data/assets/pdf_file/0024/278403/Market-Study-into-the-retail-grocery-sector-Final-report-8-March-2022.pdf at 3.182.
[56] https://comcom.govt.nz/__data/assets/pdf_file/0024/278403/Market-Study-into-the-retail-grocery-sector-Final-report-8-March-2022.pdf at pg. 324.
[57] https://comcom.govt.nz/__data/assets/pdf_file/0024/278403/Market-Study-into-the-retail-grocery-sector-Final-report-8-March-2022.pdf at pg. 343.

> **were a supplier to lose its contract with one of the major retailers, it would normally be quite difficult in the short term to replace that lost volume** with other retailers (given that these retailers would be unlikely to take on additional supplies significantly over and above their existing contracts), meaning that its own switching costs could be relatively high.

8.68 Nevo and Van den Bergh (2017) refer to large retailers as a potential bottleneck which can hinder suppliers' access to consumers:[1044]

> In modern retailing markets, **large retailers may occupy a 'bottleneck' position that allows them to control the interaction of brands**. In upstream markets, where manufacturers sell to retailers, the latter may use their superior bargaining position to extract favourable contract terms from the former. In downstream markets, where retailers sell to end-consumers, **vertically integrated supermarkets may prioritise their private labels to the detriment of branded goods. In extreme cases, powerful retailers may refuse access to the 'bottleneck'**, thus hindering the access of brand manufacturers to end-consumers.

8.69 Suppliers' lack of ability to negotiate with retailers was a key theme in responses to our supplier survey.[1045] *Examples of comments we received are listed below.*

*8.69.1 "We have two choices **1) sell to them under their terms 2) don't sell to them at all"**.* [1046]

*8.69.2 "**No ability to negotiate. We are price takers**."*[1047]

*8.69.3 "It's pretty much **sign this document, or don't supply"**.*[1048]

*8.69.4 "**Negotiations are one sided, as the retailers have all the power to either delete or keep our products on shelf**. It is a very competitive market and the supplier who gives them the most, gains the most, even if product quality suffers."*[1049]

8.70 Small suppliers may be more likely to be disadvantaged in terms of the resources and sophistication they can bring to negotiations with retailers. They may be more likely to settle for less favourable terms than suppliers with more resources.

8.71 Suppliers who lack the ability to negotiate may effectively be offered 'take it or leave it' contracts or contract terms that enable retailers to extract almost all of the value of the trading relationship.[1050] *Suppliers have little option other than to accept these terms or walk away.*

8.72 The National Māori Authority considered the current structure of the grocery market is not working well for Māori suppliers and producers of groceries. It emphasised that the major grocery retailers' use of buyer power in negotiations with suppliers extends to all producers, not just Māori. [1051]

8.73 Māori contributors told us that, in some cases, they have withdrawn their products from supply to the major grocery retailers due to narrow margins, increasing costs and expectations of promotional funding.

6.14 **The above shows that the Commission already has the evidence that it seeks, namely of market platforms, with market power imbalances, and a proposal which will exacerbated the by the proposal with the loss of options.**

6.15 **The Commission should, we submit, also consider current market developments which may make market entry less likely and / or otherwise adversely impact competition / consumers.** We note here:

a. Currently we are aware that FSNI is undertaking category reviews in which has been reported to us from suppliers that the stated aim is often a reduction in SKUs.

b. Comment has been made regarding the rollout of additional Four Square stores which has the potential to make market entry less attractive and may be seen as strategic incumbent behaviour to deter entry or make it harder.

6.16 **The proposal would also materially impact intra-group arrangements;** the FS head office would have greater bargaining power relative to individual co-operative members and greater centralisation (rationalisation) can be expected. It might also be expected to conduct itself more like FSNI, than FSSI. Comparability and options clearly reduce in a 3:2 buy-side merger (noting entry would be less, not more, likely with the proposal).

6.17 **Concluding comments:** Given the time available, we have not been able to submit in as much detail as we might have liked, however, it is clear from the above that:

a. The FS entities each operate platforms, in a highly concentrated market with limited competition.

b. They have conflicts (different incentives) as market operators, while they compete in those markets.

c. Similar platforms overseas are either regulated, being regulated, or subject to antitrust scrutiny.

d. The Commission has already determined the imbalance of power (which means the bargaining theory “distortions” apply) and these will necessarily be exacerbated by the proposal.

e. Private label’s potential for distortion was already recognised by the ACCC and the Commission, but there are growing concerns about this (we reject Houston Kemp’s assertion in the Market Study that these were only lower value commodities in NZ).

f. The reduction in options for suppliers necessarily, and as a matter of fact, reduces options, and in the circumstances can only increase market power and change incentives.

g. Not only can the Commission not be satisfied that there would be no likely SLC, but it is also clear the proposal would SLC.

7. WHOLESALE ISSUES

7.1 **We have *concerns* as to the basis for the Commission's conclusion that the *wholesale supply of groceries "is not currently a focus"*:**[58]

a. This is dismissed in two paragraphs in the SOI.[59] Further expansion of this view is necessary if we are to make submissions that would assist the Commission.

b. As noted in our earlier submission, merging 2 of 3 RGRs could frustrate parliament's legislative intent, given that FSNI and FSSI are separately listed as regulated grocery retailers in section 8 of the Grocery Industry Competition Act 2023. (Noting also that this would be a 3:2 supply-side merger of RGRs.)

7.2 **We also note:**

a. We see a clear benefit in having 3 RGRs for comparability and efficient management of the regulatory regime.

b. That said, we agree that supplier's ability to deal directly with new wholesale customers is one (and in the fact the most) important pathway under the regime.

[58] Paragraph 60 SOI.
[59] Paragraphs 59 and 60 SOI.

8. INCORRECT APPROACH TO THE COUNTERFACTUAL (IN APPLICANTS' FAVOUR)

8.1 **It is incorrect to automatically use the (posited) status quo as the counterfactual:**

a. A forward-looking approach to the counterfactual is required, and the status quo, while often useful as a starting point, is not the proper test when considering the counterfactual.

b. The SOI takes a common approach, which we submit may at times indicate subconscious bias by consistently comparing the proposal to the (stated) status quo. For example, there are references to:

i. how things "might change" comparing the status quo with the proposal;[60] and

ii. "what the Parties would likely do absent the Proposed Merger"[61]

c. This seems further compounded by the reference to a confidential counterfactual attachment to the SOI.[62]

d. This assists the applicants to argue that there would be little change, without proper consideration of whether the status quo is the appropriate counterfactual.

8.2 **This *counterfactual* approach potentially minimises the SLC / increase in market power:**

a. The Commission cannot here reach a view on counterfactuals without considering the internal mechanism (exit barriers) and why the parties do not compete.

i. Co-operative arrangements can create exit barriers and the structure of the co-operative structure should be analysed as to whether or not it is anti-competitive.

ii. FSNI and FSSI have jointly submitted that they do not compete (noting that they independently reached that view).[63] It is inconsistent to jointly submit on allegedly independent views. This begs the question of a potential cartel arrangement, and whether the reason why FSNI and FSSI do not compete is because they have reached an arrangement not to. . The current arrangement where there is sharing markets raises concerns of cartel-like behaviour.[64]

b. If the Commission chooses to not consider these issues, then there is no basis on which it can be "satisfied" when there is prima facie evidence there could be "cartel provisions" (and the arrangements within and between the two FS entities may themselves be anti-competitive).

c. The Commission cannot use a potentially illegal counterfactual as its benchmark. If it has not conducted the enquiry and reached its own view then there is no basis on

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[60] Paragraph 44 SOI.
[61] Paragraph 54 SOI.
[62] Paragraph 54 SOI.
[63] Paragraph 145 SO.I
[64] NZ-Food-and-Grocery-Council-Submission-on-Market-study-into-grocery-sector-draft-report-26-August-2021.pdf paras 1.15, 7.6 7.47, 7.13e and 7.66d; see also paragraph 7.47 which reads: *"NZFGC also recommends the Commission investigates whether agreements between Foodstuffs North Island and Foodstuffs South Island are illegal cartel arrangements."*

which it can be legitimately “satisfied” that there is no current cartel provision, or that there is no SLC arising from the merger.

d. We would be most concerned if the Commission’s stance was viewed as inaction, both as the investigator and prosecutorial body, on the basis that this is the court’s responsibility.

e. Nor should the applicants be able to benefit from a potential cartel provision and/or rely on it to demonstrate that there is no SLC.

f. The issue of potentially anti-competitive arrangements within (e.g. anti-competitive exit barriers) and between the two FS entities were clearly raised in the Market Study, including in the NZFGC submission. [65]

[65] NZ-Food-and-Grocery-Council-Submission-on-Market-study-into-grocery-sector-draft-report-26-August-2021.pdf (comcom.govt.nz).

9. RESPONSE TO SOI QUESTIONS FROM NZFGC SURVEY DATA

9.1 **Summary:** As noted above, this is one of the most significant and complex mergers that the Commission has ever considered given the grocery industry is one of the most significant markets, its function and impacts affect all New Zealanders.

9.2 Based on the information provided by our supplier members, while there are mixed views, the overwhelming majority provided to us both their views and evidence to demonstrate the very real concerns that a merger between FSNI and FSSI would likely result in a SLC in the grocery retail market for suppliers.

9.3 We submit that these concerns against a merger make sense, and these concerns would make a difference to competition, such that the Commission must confirm its preliminary view. The Commission cannot be satisfied that it will not have, or would not be likely to have, the effect of substantially lessening competition in any market in Aotearoa New Zealand.

9.4 As the Commission is aware, we undertook a comprehensive member survey based on the initial SOPI. Responses were provided through a comprehensive survey, based on the SOPI framework. This attracted 70 unique company responses, the majority of whom supply all three RGRs, and from the Chief Executive or as delegated by the Chief Executive.

9.5 Given the time constraints in this process, since submitting on the SOPI we have further analysed this information to provide greater and more detailed supplier feedback for the purposes of this submission, with a view to address with comments the Commission's questions in the SOI.

9.6 As noted supplier concerns about the ramifications of commenting mean the Commission is unlikely to get the level of responses it would like but this must not be taken to suggest those concerns are not real and abundant . We have been able to get that information to assist the Commission which we summarise below. The level of feedback, both quantitatively and qualitatively, demonstrates its evidential weight. Given concerns that comments could be used to identify parties, the comments have been paraphrased but we are happy to work through this evidence with the Commission on a confidential basis.

9.7 While we set out the survey responses in more detail below, in summary members highlighted the following concerns:

a. <u>Differences in terms and negotiations</u>: 96% say there are differences in the two FS entities operations, negotiations, or terms, 80% have different strategies between the two entities, and 88% think the proposed merger will make it harder for suppliers to do deals directly with individual stores/groups of stores/banners.

b. <u>Increased market power</u>: 71% believe the status quo of three RGRs assists negotiations more than the proposal; 77% think the merged FS could have a greater ability to depress prices paid to supplier.

c. <u>Other impacts</u>: 76% have concerns about impacts in other parts of the supply chain and/or greater costs being imposed on suppliers.

d. <u>No consumer benefit</u>: 74% do not expect any merger-specific 'cost savings' (lower prices from suppliers) to be passed on to consumers and 55% think the proposal would make it harder for suppliers to negotiate pass-through.

e. Members also thought that the proposal would make new retail entry (or expansion by small/niche players) less likely with 74% believing it would make it harder.

9.8 The statements from suppliers highlight issues with the impact of the proposed merger on supply arrangements and competition generally.

a. **Reduced Options for Suppliers:** Suppliers share the view that a merger would reduce the number of Regulated Grocery Retailers (RGRs) from three to two, limiting options for suppliers and potentially increasing their dependence on the merged entity. This could result in decreased bargaining power for suppliers and fewer opportunities for innovation and differentiation. Suppliers believe that maintaining three RGR options reduces risks by providing more negotiation leverage and spreading business across multiple entities. They feel that a merger would increase risk, especially for SMEs, due to the dominance of a merged entity.

b. **Barriers to Entry and Market Dominance:** Suppliers share the view merging the market share and power into one entity, the merger could create significant barriers to entry for new market players and smaller suppliers, further consolidating the market power of the merged entity. Suppliers express concerns about the dominance of FSNI and FSSI in the market, which could deter competition and innovation in the long term.

c. **Supplier Relations and Terms:** Suppliers highlighted the experienced market-dominant negotiation tactics of FSNI and express concerns that these practices will worsen post-merger. Even with the new protections of the Code they anticipate increased pressure for additional investment and unfavourable terms, potentially leading to decreased profitability and viability for suppliers, especially smaller businesses.

d. **Impact on Volume and Supplier Base:** While there is agreement that the overall volume of groceries may not be affected by the merger, there are concerns about the potential for major variations at the supplier level. This includes the possibility of supplier profitability reduction, product deletions, and increased costs of doing business.

e. **Risk of Reduced Choice and Innovation:** Suppliers express concerns about the potential adverse effects on innovation and new product development due to the merger. They indicate concern that the merged entity's focus and increased negotiation power could stifle innovation and limit opportunities for smaller suppliers and new market entrants. They are wary that decisions driven by retailer margin and lowest cost might limit innovation and reduce supplier profitability, ultimately stifling competition and consumer choice. Suppliers also felt the merger could lead to reduced product choice and innovation for consumers, as suppliers may face challenges in getting new products ranged and promoted. This could limit consumer options and hinder market dynamism and competition.

10. COUNTERVAILING POWER OF SUPPLIERS

10.1 While the Commission's SOI[66] asks for evidence of the countervailing power of suppliers of grocery products to the Parties in markets in which the Parties acquire grocery products, we were provided little evidence of this in the survey feedback or member information that we received but did receive an abundance of evidence to the contrary.

10.2 The sentiment, views, and experiences shared suggest that the suppliers perceive themselves as having less negotiating power relative to the acquiring parties, and they express concerns about potential imbalances in power dynamics resulting from mergers or consolidation within the grocery retail sector. This indicates that suppliers are aware of their limited countervailing power and its marginal impact on negotiations and market dynamics.

10.3 The sentiments shared by suppliers in the provided statements revolve around concerns regarding the consolidation of power within retail groups, particularly in the context of potential mergers or centralisation of business operations. Suppliers express apprehension about the increased negotiating power of these retail entities, which could lead to higher costs of doing business for suppliers and potentially increased prices for consumers. They highlight the risks of a duopoly or consolidation of market power, which could result in reduced negotiation leverage for suppliers and limited consumer choice. Additionally, suppliers express concerns about the potential for margin pressure, reduced profitability, and the possibility of being marginalised within the market. Overall, they emphasise the need to maintain a balance of power and choice within the retail landscape to ensure fair and competitive business practices.

10.4 The survey provided evidence that there is strong potential for the merged entity's buyer power to manifest in both unilateral and coordinated effects within upstream markets for acquiring groceries. Suppliers expressed concerns over the substantial reduction in the number of RGR entities post-merger, indicating that the consolidated entity would wield considerable bargaining power. This concentration may enable the merged entity to impose more favourable terms on suppliers, including increased margins, merchandising costs, and additional investments, as noted in various statements.

10.5 Furthermore, the potential for exit by suppliers from the acquisition market, driven by concerns over profitability and increased costs of doing business, underscores the significant impact the merged entity's buyer power could have. Additionally, the statements suggest that the merger could result in a reduction in the number of channels available to suppliers, limiting their options and potentially reducing their bargaining leverage in negotiations.

10.6 We have provided a summary of the comments provided to us in our member survey addressing this point. Each comment has been summarised and anonymised, to avoid identification of any individual supplier:

i. The supplier anticipates that granting more power to the retailers will exacerbate the challenges they already face in negotiations.

[66] Paragraph 24.4, countervailing power of suppliers of grocery products to the Parties in markets in which the Parties acquire grocery products the countervailing power of customers.

ii. The supplier believes the larger the retail grocery retailers (RGR), the more dominant their negotiating power becomes.

iii. The supplier notes that the centralisation of business operations translates to centralised power, potentially reducing suppliers' negotiation leverage and leading to increased costs for them and higher prices for consumers.

iv. The supplier believes the merger would elevate the influence of the FS group, posing a larger risk to suppliers' businesses if agreements cannot be reached.

v. The supplier states the consolidation to two RGRs strengthens their negotiating power while weakening that of suppliers.

vi. The supplier is concerned that the buying model concentrates decision-making authority on ranging, promotions, and display into the hands of a single entity, amplifying the power of the RGR.

vii. The supplier believes the availability of FSSI acts as a counterbalance to centralised power, but its integration into the same system post-merger diminishes this foil.

viii. The supplier states reducing to two RGRs in New Zealand increases the market power of the remaining RGRs.

ix. The supplier believes a merger would establish a duopoly, significantly amplifying the power imbalance.

x. The supplier notes the current power imbalance in favour of the RGRs will intensify with the merger, exacerbating the challenges for suppliers.

xi. The supplier finds that having three options provides suppliers with more flexibility, mitigating the risk if one retailer declines their products.

xii. The supplier believes that previous practices of cutting range and demanding higher funding, coupled with increased margins, pose significant risks that would escalate with the merger of the two entities.

xiii. The supplier believes a merged entity would possess stronger negotiating power, likely resulting in further range rationalisation, reduced consumer choice, and higher costs for suppliers.

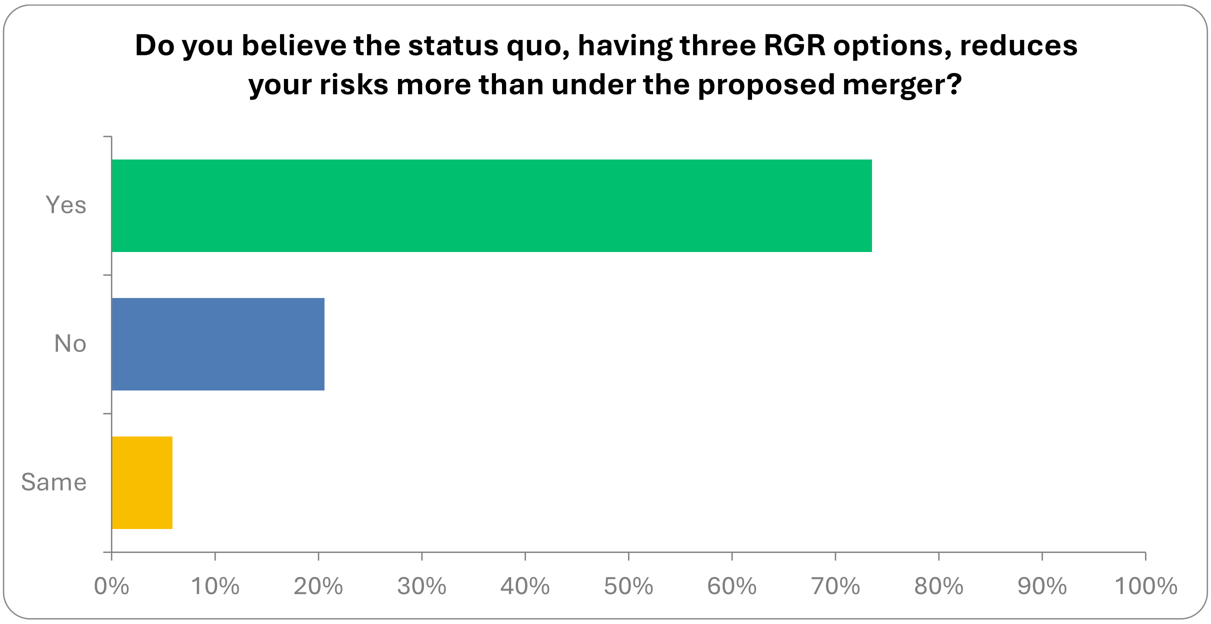
xiv. The supplier feels the combined entity's consolidated power would enable the combined entity to negotiate more assertively, resulting in winners and losers among suppliers.

11. MERGER IMPACTS

11.1 The SOI discusses and seeks further consideration of the impacts of the proposal and if there would be a SLC considering several factors set out in paragraphs 39 and following: transfer of surplus from supplier to ME, reduction in choice and quality, exit by suppliers from the acquisition market, reduction ins number of channels, reduction in suppliers' ability and incentive to innovate within a bargaining framework, and whether a SLC may be likely if the proposed merger results in any of the above.

11.2 Suppliers express deep concerns about the current and further consolidation of power within the grocery retail sector, indicating a scenario where an even smaller number of buyers would wield significant influence over negotiations and market dynamics. Comments highlight the apprehension towards a situation where a limited number of buyers hold substantial market power. Furthermore, statements emphatically underscore the perception of a concentration of power in the hands of the acquiring parties, which could severely limit suppliers' bargaining leverage.

FIGURE 1.



11.3 Most suppliers believe that the merger would further tilt the balance of bargaining power in favour of the merged entity, allowing it to negotiate more favourable terms to the detriment of suppliers.

a. **Increased Market Dominance:** Suppliers expressed concern that the merged entity would be a significant consolidation. They were concerned about their ability to negotiate diminishing and the merged entity having more control over pricing and terms of trade and leading to a transfer of surplus from suppliers to the merged entity.

b. **Supplier Dependency:** Suppliers were concerned about becoming increasingly dependent on the merged entity for access to the grocery retail market. This dependency would further weaken supplier bargaining position, as many expressed reluctances to risk losing access to a significant portion of their sales by challenging unfavourable terms imposed by the merged entity – even under the status quo.

c. **Risk of Price Squeeze:** Suppliers also raised concerns that there is risk of further 'price squeeze' strategies, where the merged entity will reduce the margins it pays to suppliers while simultaneously maintaining or increasing retail prices for consumers. This would further erode supplier profitability and create barriers to entry for new competitors, exacerbating the lessening of competition in the market.

d. **Impact on Innovation and Investment:** A transfer of surplus from suppliers to the merged entity may also result in reduced investment in innovation and product development. Suppliers raised this and indicated that in facing further squeezed margins they would have little to no resources available to invest in research and development, leading to a stagnation in local product offerings and a reduction in consumer choice and variety.

e. **Exit from Market:** There remains the possibility of suppliers exiting the acquisition market if the proposed merger results in unfavourable terms or reduced profitability. With fewer retail options due to consolidation, suppliers may face increased pressure from the merged entity's, leading some to withdraw from supplying to the market altogether.

12. ENTITY COMPARSION

12.1 The SOI discusses and seeks further consideration of the impacts of how suppliers have reacted in the past when the major grocery retailers have changed their price or other terms relating to the acquisition of groceries[67] and SOI sets out evidence surfaced to date in the following paragraphs.[68]

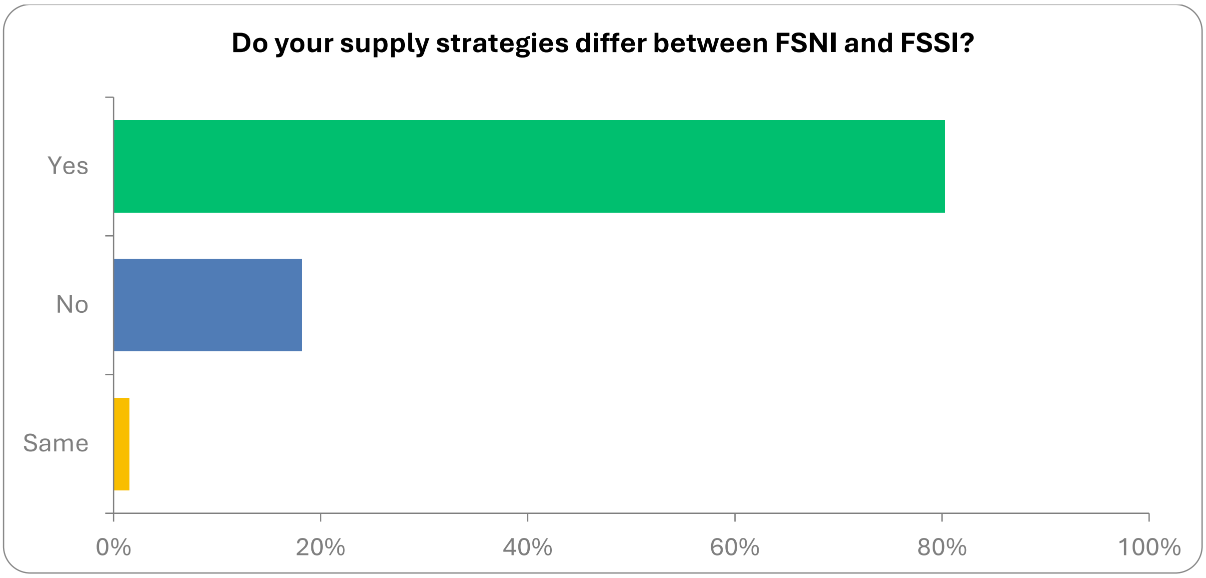
12.2 Suppliers raised the following issues for consideration:

a. **Impact on Trading Practices**: Suppliers are concerned that if FSSI adopts the FSNI way of working, they would lose the ability to trade at store level, affecting their ability to offer discounts and negotiate terms.

b. **Short-term Risks and Long-term Efficiencies:** While suppliers anticipate long-term efficiencies from the merger, they acknowledge short-term risks due to differences in cost price and ranging between FSNI and FSSI. Additionally, they note concerns about retailers cutting range, increasing demands for funding, and exerting more control over individual stores, which could exacerbate if the entities merge.

c. **Changes in Relationships:** Suppliers highlight an assertive approach of FSNI in asking for additional investment to do business, including increased terms, margins, and merchandising costs. They cite instances of deranging in the South Island and North Island, which have impacted their operations. Suppliers express concerns about the risk of cherry-picking by FSNI, where the retailer pressures for untenable terms, potentially worsening under a merged entity.

FIGURE 2.



d. We have summarised and anonymised the following comments related to this point:

i. The supplier highlights the difference in trading practices between FSNI and FSSI, expressing concern that adopting the FSNI's approach post-merger would limit their ability to trade at the store level. They provide a specific

[67] Paragraph 73.2 SOI.
[68] Paragraphs 87.1, 87.2, 89 SOI.

example where they learned from negotiation experiences to secure more favourable terms, which may become challenging if the merger aligns practices across regions.

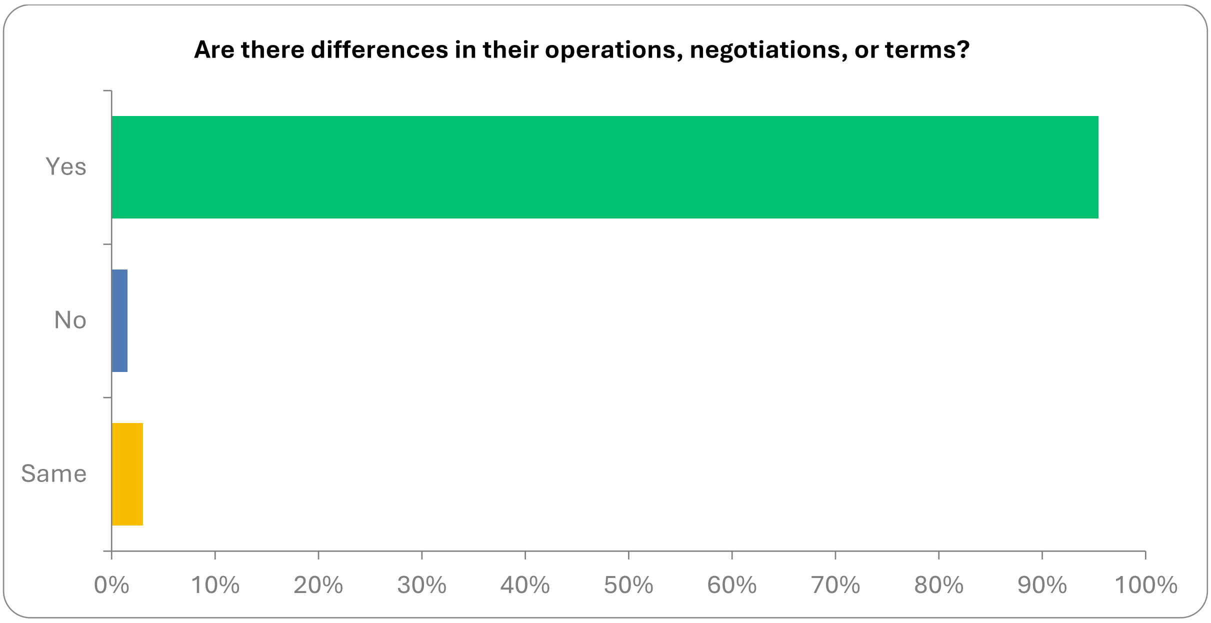
ii. The supplier acknowledges the potential long-term efficiencies from the merger but identifies short-term risks for their business stemming from differences in cost prices and ranging between FSNI and FSSI.

iii. The supplier expresses concern about retailers' increasing control over stores, with owner operators' minimal control on range, price, and display decisions. They also discuss that there are greater funding demands placed on suppliers, which could escalate if the merger proceeds. They are concerned that retailers are already placing higher demands for funding, with margins are increasing and any expected price reduction to the consumer funded by the supplier.

iv. The supplier assesses FSNI's approach, describing it as aggressively seeking additional investment from suppliers through increased terms, margins, and merchandising costs, which poses a further risk if this approach extends to FSSI post-merger.

v. The supplier highlights the risk of "cherry-picking" by FSNI, suggesting that their dominant position in the market enables them to pressure suppliers for unfavourable terms, a situation that may worsen post-merger.

FIGURE 3.



13. IMPACTS ON SUPPLY TERMS AND ALTERNATIVES

13.1 The SOI invites further evidence on the supply terms, volume comparisons, and information on alternatives available to suppliers.

13.2 Suppliers largely agree that while the overall volume of groceries acquired by the parties may not change significantly, there were concerns about notable shifts at the supplier level due to various factors such as supplier profitability reductions, product deletions, and increased business costs. They anticipate potential variations in supplier volumes driven by negotiation outcomes, leading to consolidations within the supply base.

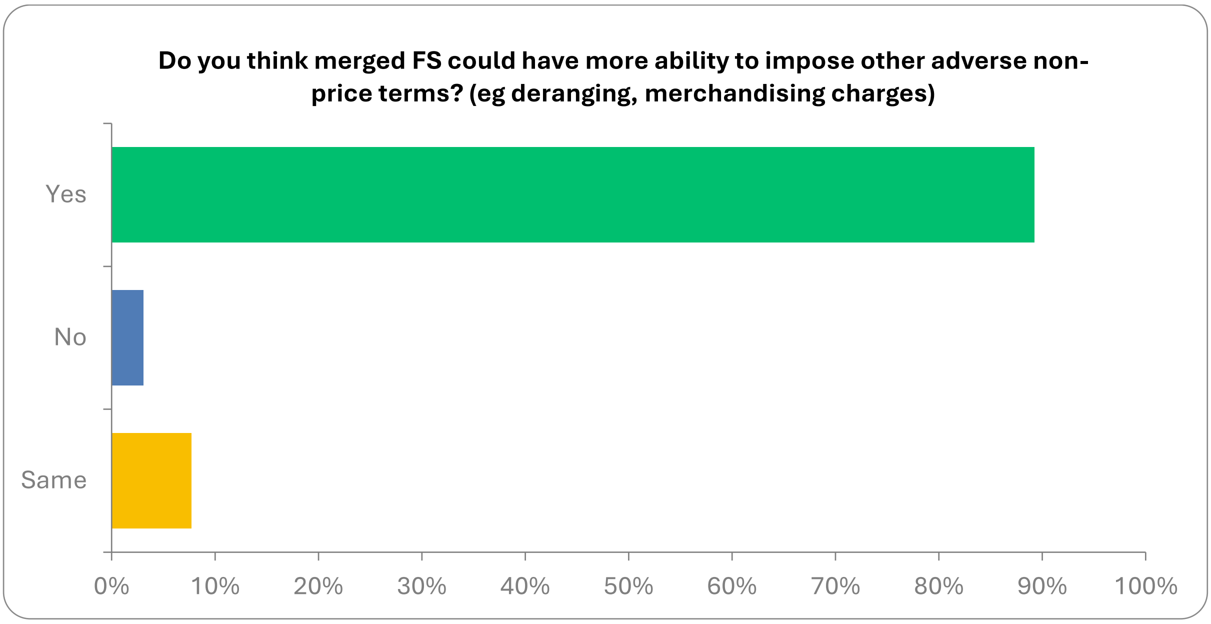
13.3 Suppliers believe that maintaining three separate retailers reduces risks by offering more options and spreading the risk, and that the merger would significantly increase risk due to reduced options and potential dominance by the merged entity.

13.4 Suppliers generally perceive non-regulated retailers like TWG and Costco are too small to have a significant impact or provide a viable alternative to the major retailers. While some have trading relationships, they believe these alternatives lack the scale to compete effectively with the main retailers.

13.5 Suppliers told us that they currently have a mix of agreements for supply. There were comments that agreements between the two FS entities had variations in trading terms, promotions, and day-to-day operations between different regions, which could potentially pose challenges for the merged entity in harmonising supply arrangements across different categories or geographies.

13.6 While many agree that the overall volume of groceries acquired by the parties won't change significantly, concerns linger regarding the potential impact on local suppliers. Some are concerned that national ranging decisions resulting from the merger could disadvantage smaller, local suppliers, leading to variations in supplier volumes and potentially driving some out of business due to increased costs and product deletions.

FIGURE 4.



13.7 Moreover, suppliers express apprehension about the concentration of power in a duopoly scenario, emphasising the benefits of having three separate businesses to deal with instead of two. They argue that this diversification of business relationships helps spread risk more effectively, especially considering the challenges associated with market consolidation. Additionally, suppliers highlight the importance of maintaining regional focus for local suppliers. Overall, while some see some possible benefits in the merger, others remain wary of its implications for supplier viability and market competition.

13.8 Below are comments provided through the survey, characterised and anonymised. These comments cover off supplier's views on market dynamics, negotiations and core ranging, relationships, risk and competition, and market alternatives.

i. The supplier is concerned that local suppliers might lose out due to national ranging decisions.

ii. The supplier anticipates that total volume would remain the same, but there may be major variations at the supplier level, impacting profitability and leading to business closures.

iii. The supplier anticipates a shift in supplier volumes due to negotiation outcomes, though not necessarily at a total level.

iv. The supplier believes the merger will impact where the volume of groceries is sourced from.

v. The supplier suggests that while total volumes of categories might not be affected, volumes across the supplier base will change, leading to supply base consolidation.

vi. The supplier believes that if successful in achieving core ranging with FSSI to the same level as FSNI, there may be enhanced margins due to additional volume but is not sure if likely.

vii. The supplier mentions supplying the Warehouse (TWG) and Costco, among other channels, but acknowledges they represent much smaller volumes.

viii. The supplier believes they have greater ability to drive volume through more trading partners as a benefit of the current setup.

ix. The supplier emphasises the advantage of dealing with three separate businesses rather than two, citing challenges associated with market concentration.

x. The supplier discusses the economic viability and consumer impact of different ranging models across FS banners if applied across the board.

xi. The supplier is concerned that there will be a consequence for the consumer as they don't believe it will be feasible to continue to offer unique product.

xii. The supplier states that if the 'new' FSNI model of ongoing SKU unit funding was applied nationally, the range and variety in the category would be reduced significantly.

xiii. The supplier discusses that the status quo reduces risks as each entity has a different (and separate) decision maker, business strategy (including pricing and funding) and set of business values.

xiv. The supplier expresses concerns about increased risk if core ranging options are reduced to two from three RGRs.

xv. The supplier foresees a duopoly and increased imbalance of power resulting from the merger.

xvi. The supplier stresses the ability to spread risk more readily with three RGR options.

xvii. The supplier believes that having three options in ranging and negotiations reduces the potential dominance of larger suppliers.

xviii. The supplier views the status quo as reducing the risk of deletion or lessening its impact.

xix. The supplier describes the challenges faced by retailers cutting range and making higher demands for funding.

xx. The supplier affirms that supplying to three RGRs is better for spreading risk.

xxi. The supplier expresses concern about increased leverage over suppliers and costs associated with a merged FS entity.

xxii. The supplier believes there are more ranging options and routes to market currently.

xxiii. The supplier highlights differences in business decision-making processes between FS entities and their impact on ranging.

xxiv. The supplier sees reduced risk of losing significant business with three RGR options but notes administrative challenges.

xxv. The supplier raises concerns about reduced category competition and consumer choice if category rationalisation occurs.

xxvi. The supplier views non-regulated retailers like TWG and Costco as lacking the scale to have a significant impact.

xxvii. The supplier describes non-regulated retailers as small and insufficient to offset risks or significant reduction in grocery volumes.

xxviii. The supplier indicates limited volume and significance of non-regulated retailers compared to RGRs.

xxix. The supplier believes the volumes in non-regulated retailers are too small to be material competitors.

xxx. The supplier highlights the potential for a new grocery retailer to emerge because of the merger.

xxxi. The supplier notes that alternatives lack comparable scale to main retailers.

xxxii. The supplier considers non-regulated retailers as options but small compared to RGRs.

xxxiii. The supplier acknowledges the limited impact of non-regulated retailers on grocery volumes.

xxxiv. The supplier describes non-regulated retailers' volumes as minor in the scheme of things.

xxxv. The supplier indicates that the balance of the market is inconsequential.

xxxvi. The supplier mentions the small financial impact of non-regulated retailers.

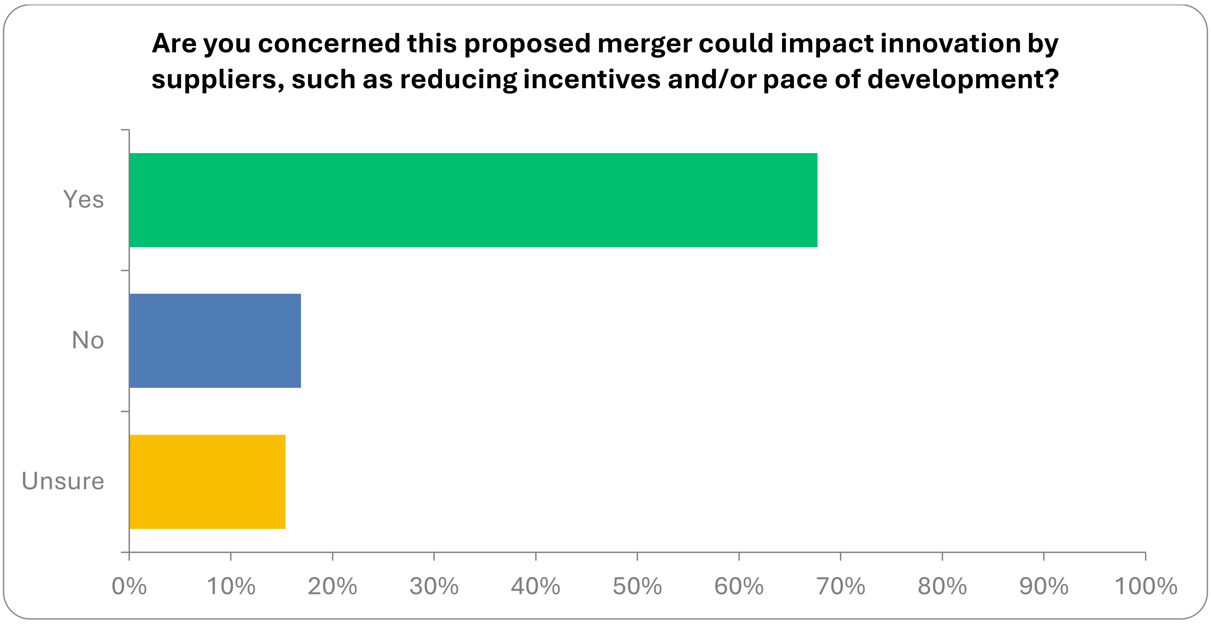
14. IMPACTS ON INVESTMENT IN INNOVATION

14.1 The SOI asks several questions about the impact on investment on innovation, paragraphs 102 and following, and invites suppliers to provide further information on whether a reduction in price is likely to affect investment in innovation given that "increase in buyer power may also reduce suppliers' ability and incentives to invest in new and innovative products, due to reduced profitability."[69]

14.2 The member survey raised about potential adverse effects on supply, ranging, quality, and innovation due to tighter margins and reduced pricing flexibility. Additionally, increased costs of doing business could impact the attractiveness of the market for investment, potentially jeopardizing the long-term viability of the industry. When asked you concerned this proposed merger could impact innovation by suppliers, such as reducing the incentives and/or pace of development, 68% of suppliers answered yes.

14.3 Overall, the statements suggest that a reduction in prices resulting from the proposed merger would have a negative impact on investment in innovation. Tightened margins, squeezed pricing, and increased pressure on profitability may limit resources available for innovation initiatives and hinder the innovation process.

FIGURE 5.



14.4 The statements provided offer insights into how a potential reduction in prices, stemming from the proposed merger, could impact investment in innovation:

a. **Impact on Innovation:** Some believe it may lead to greater investment and efficiency in the innovation process, while the majority were concerned about the increased pressure on margins and reduced supplier ability to take risks in new product development.

[69] Section 102 of SOI.

b. **Margin erosion:** Suppliers express concerns about working on tight margins and the erosion of cost pricing. This suggests that any reduction in prices could further tighten margins, leaving little room for investment in innovation.

c. **Squeezed pricing:** Some suppliers mention that innovation is key but is hindered by squeezed pricing. This indicates that a reduction in prices may limit resources available for innovation efforts.

d. **Chilling effect:** There are concerns that the merger could have a chilling effect on innovation, particularly if decisions are solely based on retailer margin and lowest cost. This suggests that a focus on reducing prices may divert resources away from innovation initiatives.

e. **NPD impacts:** The majority are concerned that increased pressure on margins could reduce supplier ability to take risks in new product development. This indicates that a reduction in prices may lead to reduced investment in innovation due to risk aversion.

f. **Profitability:** Suppliers express concerns about decreased profitability and increased risk of ranging, leading to reduced innovation. This suggests that a reduction in prices may lead to decreased profitability, making it challenging to allocate resources to innovation efforts.

g. **Change in Product Mix:** Expectations include a greater emphasis on private label products, potentially limiting brand diversity and stifling innovation. There is a consensus that the product mix and ranging strategies will continue to evolve.

h. **Market Entry and New Product Development (NPD):** Views vary on the ease of entering the market or launching new products with FSSI, with some finding it more open to innovation and supportive of local manufacturers. Others express challenges in entering the market or getting products accepted by FSNI.

i. **Cost Concerns:** Pressure on costs is expected to limit innovation and marketing support for new products, alongside the risk of limited market access.

j. **Other Concerns:** Concerns include potentially less choice and innovation, as well as the risk of increased negotiation pressures at the expense of innovation and barriers to entry for small businesses. Additionally, the consolidation of market players raises concerns about significant changes in the retail landscape and the investment in future innovation.

k. The following comments are from individual suppliers that have been summarised and anonymised for this submission:

   i. The supplier expresses concerns about tight margins and potential erosion of cost pricing affecting product supply, range, quality, and innovation negatively.

   ii. The supplier believes innovation may suffer due to pricing pressures, limiting resources available for innovation initiatives.

   iii. The supplier thinks the proposed merger might not negatively impact innovation, ranging, quality, or innovation and could lead to improvements given efficient national range.

iv. The supplier notes FSSI's more flexible approach to New Product Development (NPD) processes.

v. The supplier expresses concern regarding potential reductions in innovation.

vi. The supplier worries that the proposed merger could stifle innovation and new product development in New Zealand, affecting both local and international markets.

vii. The supplier anticipates increased costs of doing business could deter global investment in innovation, sustainability, and local manufacturing, impacting industry viability.

viii. The supplier anticipates a decrease in new product development and innovation over time due to increased costs and business challenges.

ix. The supplier predicts a greater emphasis on private label products, potentially.

x. The supplier expects changes in ranging and NPD processes over time.

xi. The supplier recognises pros and cons regarding retailer influence on NPD decisions, with potential challenges in negotiations.

xii. The supplier perceives that the proposed merger won't significantly impact innovation due to existing challenges and market power dynamics.

xiii. The supplier notes the significant influence a retailer with a 60% market share holds over innovation decisions.

xiv. The supplier expects greater investment requirements and margin squeezes impacting innovation and risk-taking.

xv. The supplier believes that the proposed merger will improve the innovation process through more consolidated and efficient national ranging.

xvi. The supplier provides an example of past innovation acceptance discrepancies between FS entities, with concerns about losing diversity in commercial focus post-merger. A new, innovative offer was accepted by one FS entity, but not by the other FS entity. After positive performance, the other FS entity accepted the range later. If the first FS entity had not accepted the innovation, the products would not now be on the market. Currently, there is diversity in commercial focus and concern that this will disappear if FS merge.

xvii. The supplier foresees impacts of reduced profitability and increased risk on innovation levels.

xviii. The supplier acknowledges that high-pressure environments can sometimes drive greater innovation needs.

xix. The supplier highlights efforts in conducting specific ranges in the South Island to test and learn.

xx. The supplier notes FSSI for being more open to innovation and supporting New Zealand manufacturers compared to FSNI, with better speed to market.

xxi. The supplier observes that FSSI tends to be more receptive to smaller players and new ideas compared to FSNI.

xxii. The supplier shares experience indicating that FSNI has been more amenable to new product trials recently.

xxiii. The supplier predicts limitations on innovation and marketing support due to cost pressures and market access risks.

xxiv. The supplier expects potentially reduced choice and innovation frequency, balanced against potential profit gains for the merged entity.

xxv. The supplier expresses concerns about increased risk and barriers to entry for small businesses due to anticipated changes in the retail landscape.

xxvi. The supplier foresees impacts of harder commercial negotiations on innovation and barriers to entry for small businesses.

15. PREVIOUS MERGER EXPERIENCE

15.1 The SOI considers the extent to which the previous merger between FS Auckland and FS Wellington in 2013 resulted in efficiencies and/or cost savings on the supply-side.

15.2 Suppliers told us they experienced a shift towards centralised decision-making, with the new entity exerting dominance in negotiating better terms. Negotiations often favoured the terms where there was the lowest cost, resulting in reduced profitability for some suppliers. Of those that could comment, 53% said it had been harder following the 2013 FSNI merger, with higher prices.

15.3 Efforts to centralise operations and consolidate decision-making led to challenges for suppliers, particularly in navigating the dominance of the new entity. While some efficiencies were realised, such as streamlined communication and reduced FS duplication, concerns were raised about the impact on prices and profitability for suppliers.

15.4 Lessons learned from the previous merger highlight the potential implications for the proposed merger between FSNI and FSSI. Suppliers expect that the business model of FSNI will prevail post-merger, with centralised decision-making and cost reduction measures likely to be implemented. Suppliers are concerned about a repeat of the previous merger's outcomes, with increased pressure on margins and limited innovation in product offerings.

15.5 Despite the promises of increased efficiencies and cost savings many commented that the previous merger failed to deliver tangible benefits to consumers, with prices sometimes increasing and ranging opportunities decreasing. Suppliers faced challenges in maintaining profitability amidst increased competition and reduced bargaining power. The proposed merger impact extends beyond the supply-side, affecting consumer choice and market dynamics.

15.6 Suppliers express concerns about the potential negative consequences of the proposed merger on competition and supplier innovation. Supplier noted that there was evidence of some efficiencies and cost-savings resulting from the merger of Upper North Island (UNI) and Lower North Island (LNI) but that these efficiencies and cost-savings often came at the expense of suppliers. Some specific examples include:

a. **Reduction in FS duplication**: Removal of duplication was mentioned as a positive outcome of the merger, suggesting streamlining of FS processes and reduction in redundant activities.

b. **Centralised negotiation leverage:** The merger allowed for centralised negotiation leverage, enabling the combined entity to exert pressure on suppliers and secure more favourable terms.

c. **Reduction in headcount:** Consolidation of key account teams resulted in a reduction in headcount, leading to cost savings for the merged entity.

d. **Improved distribution efficiency:** There were mentions of improved distribution efficiency post-merger, indicating potential logistical benefits, although noting that that 70% of supplier believed that there could be changes in the distribution centre arrangements, such as increasing costs and fewer options, that could adversely impact them.

15.7 However, while these efficiencies and cost-savings were achieved, there were also adverse effects noted, such as:

a. **Increased prices and reduced choice:** Many comments highlighted consumer price increases and reduced product choice post-merger alignment, suggesting that cost savings may not have necessarily translated into lower prices for consumers.

b. **Supplier margin compression:** Suppliers often bore the brunt of negotiations, experiencing decreased profitability due to margin compression and increased demands from the merged entity.

c. **Negative impact on local suppliers:** Centralised pricing reports and negotiation tactics negatively impacted local suppliers, leading to market exits and loss of benefits associated with local supply chains.

15.8 Comments summarised and anonymised:

i. The supplier recalls changes included harmonising terms, highlighting the criticality of ranging decisions, and absorbing fixed costs.

ii. The supplier compares that the costs between Upper North Island (UNI) and Lower North Island (LNI) were more aligned indicating an easier transition to the proposal.

iii. The supplier recalls that there was a perceived dominance of the larger UNI business and that post-merger this allowed for alignment in outcomes, policies, procedures, and management.

iv. The supplier mentions there was alignment to one dedicated team tasked with securing the best terms from suppliers but at significant cost to them.

v. The supplier observes slower change in fresh produce compared to other categories during the alignment process.

vi. The supplier was required to adjust terms based on the highest among the merging entities.

vii. The supplier notes assertive negotiation tactics by the UNI, and believes it led to increased margin without benefit.

viii. The supplier notes that there as a ME strategy to identify and secure the best terms across both Lower and Upper stores for the buyer.

ix. The supplier notes there was a transition to greater control by head office, evidenced by the introduction of a centralised SAP system.

x. The supplier witnessed challenges in cultural integration post-merger, despite potential improvements in discussions.

xi. The supplier acknowledges changes in trading arrangements, but that terms were already common.

xii. The supplier reflects on better past options for product placement and risk spread, compared to the current scenario.

xiii. The supplier anticipates similar experiences lessening supplier leverage if the proposed merger proceeds.

xiv. The supplier predicts the FSNI model prevailing post-merger, impacting business practices, policies, and culture.

xv. The supplier compares the proposal with other mergers, where they found that cost reductions didn't necessarily translate to lower prices for consumers.

xvi. The supplier notes positive outcomes regarding ranging improvement for Lower North Island (LNI) post-merger.

xvii. The supplier identifies benefits and detriments of consolidation, including decreased profit for suppliers and increased reliance on the merged entity.

xviii. The supplier highlights alignment of terms, leading to increased supplier investment and centralised negotiation leverage.

xix. The supplier noted that the ME combined volume leverage to secure favourable terms, taking the lowest net price, added cost, and voided historical agreements in place.

xx. The supplier mentions consumer price increases and reduced product choice post-merger alignment.

xxi. The supplier describes the impact on product range and pricing post-merger alignment.

xxii. The supplier notes resource limitations and negotiation challenges since the ME and reduced own head count.

xxiii. The supplier shares an example of the negative impact on local suppliers due to centralised pricing reports and negotiation tactics.

xxiv. The supplier shares an experience of negotiations favouring higher terms post-merger alignment.

xxv. The supplier compares merchandising approaches noting increased alignment post-merger.

xxvi. The supplier mentions range consolidation and product deletions post-merger.

xxvii. The supplier notes improvements in distribution but rationalisation of range post-merger.

xxviii. The supplier describes adverse impacts on terms and retailer margins post-merger alignment.

16. CENTRALISATION IMPACTS ON NEGOTITATION

16.1 The SOI discusses that the proposed merger would "enable this process of centralisation to accelerate and a move to a more centralised model would mean the loss of an opportunity and flexibility to negotiate at the store level, and overall, one less opportunity to negotiate entry to the market"[70] and discusses "there are also some participants who consider that there are benefits to dealing with one entity, as opposed to any negotiations taking place at a store level, due to enabling them to streamline processes and the efficiency of doing business".[71]

16.2 The sentiment from suppliers is that this further centralisation and concentration would present upward challenges for suppliers. The concentration of decision-making power at the national level and the potential homogenisation of terms could further restrict supplier autonomy and diversity within the market.

16.3 Many suppliers noted their view that there were centralisation efforts already underway, impacting pricing negotiations and leading to downward pressure on prices. This trend, coupled with the potential merger, poses challenges for smaller suppliers, raising barriers to entry and reducing consumer choice. We had feedback that told us direct dealings with stores are becoming increasingly difficult and harder to do, particularly in regions where centralisation is already occurring, and this challenge is expected to intensify post-merger.

16.4 As the operating model of the merged entity is likely to be greater centralisation, further consolidating decision-making power is expected at the national level. Additionally, the consolidation likely removes decision-making autonomy from local levels, limiting investment opportunities and decision-making to a single entity.

16.5 Suppliers believed that the current availability of the FSSI is a counterbalance to centralised power and worry that its integration into the merged entity would further exacerbate this.

16.6 Here are comments from the survey, summarised and anonymised:

i. The supplier believes centralisation in current negotiations are already leading to the depression of prices, suggesting that further centralisation, such as through a merger, could exacerbate this trend.

ii. The supplier is concerned a merger could increase barriers to entry for smaller suppliers, limiting innovation and resulting in less choice for consumers. This trend is already evident in discussions around centralisation.

iii. The supplier believes that he centralisation initiatives in the North Island are already making it harder to deal directly with stores. A merger could worsen this situation, potentially limiting supplier access to individual stores.

iv. The supplier states that a national template post-merger is likely to mirror the centralisation already seen in the FSNI operating model.

v. The supplier discusses the CPT business model, which centralises decision-making and funds, removes the ability to invest at the local level. This

[70] Paragraph 116 SOI.
[71] Paragraph 116 SOI.

centralised power may restrict stores from promoting or displaying non-core ranged items, and a merger would likely integrate FSSI into this system.

vi. The supplier discusses variances in net costs to stores due to differing terms and centralisation models result in different promotional discounts and retailer margins, potentially complicating supplier relationships and strategies.

17. INCREASE OF BUYER POWER AND PRIVATE LABEL

17.1 The SOI asks whether the Proposed Merger could lead to an increase in buyer power and afford the merged entity a greater ability and incentive to increase the penetration of private label products, and whether this would have a negative effect on competition.[72]

17.2 The proposed merger raises concerns among suppliers regarding its potential impact on buyer power and the proliferation of private label products. Suppliers anticipate that the merged entity would pivot towards private label offerings, shifting away from traditional suppliers and reducing consumer choice in the process. With a likely emphasis on private label brands such as Pams, suppliers are concerned that the merged entity would gain greater control over product lines, stifling innovation, and investment in branded products.

17.3 Already several suppliers have noticed the increased activity of private labels, including recent high-profile marketing as "New Zealand's favourite brand".

17.4 Furthermore, the proposed merger could disrupt existing supplier arrangements, with the merged entity potentially favouring national contracts and sourcing more private label products. This shift raises concerns about the difficulty of local New Zealand companies, which may face unfavourable terms or even exclusion from supplying private label goods. Suppliers also anticipate this will stifle innovation for the development of new products given the focus on private label lines.

17.5 The consolidation of buyer power under the merged entity could also lead to adverse effects on competition within the market. As private label products are prioritised and proprietary brands are rationalised, consumer choice may diminish, leading to reduced product competition and innovation in affected categories. This trend could result in higher retail pricing for products and a less diverse market landscape, ultimately disadvantaging both consumers and smaller suppliers.

17.6 Overall, the proposed merger is seen as a harbinger of increased buyer power and a shift towards private label dominance. Suppliers are concerned the potential consequences for competition, innovation, and their own businesses, highlighting the need for careful consideration and regulatory scrutiny of the merger's implications.

i. The supplier anticipates the applicants may prioritise private label over other suppliers, potentially leading to a more limited range for consumers.

ii. The supplier expects a greater emphasis on private label products post-merger, giving the RGR greater control but potentially stifling innovation and brand investment.

iii. The supplier anticipates the merged entity might shift towards sourcing more private label products, potentially disadvantaging New Zealand companies.

iv. The supplier believes the proposed merger's impact on private label goods varied, with comments highlighting current sourcing methods and potential changes in contract sizes, according to the supplier.

[72] Paragraph 117 SOI.

v. The supplier considers that current supply methods involve national buying and contractual agreements for private label products.

vi. The supplier believes the proposed merger may result in increased pressure to convert products to private label or introduce new private label items.

vii. The supplier thinks there may be alignment of supply may occur, especially for fresh products, to secure lower pricing.

viii. The potential impact on fresh produce supply simplification and regional challenges remains uncertain, according to the supplier.

ix. The supplier states that greater volume and leverage would be used to reduce price.

x. The supplier considers possibility of further national tender for Pams products, potentially favouring large-scale corporate producers, as at a volume that they would not be able to supply.

xi. The supplier considers that private label products may experience increased growth rates compared to branded items.

xii. The supplier anticipates the rationalisation of proprietary brands may lead to the expansion of private label products, according to the supplier.

xiii. The supplier considers that it is possible that there may be more focus on private label products but note FSSI and FSNI have different approaches.

xiv. The supplier notes that private label products are the priority for FS.

xv. The supplier believes there is a possibility of worsened terms post-merger.

18. NEW MARKET ENTRY OR EXPANSION

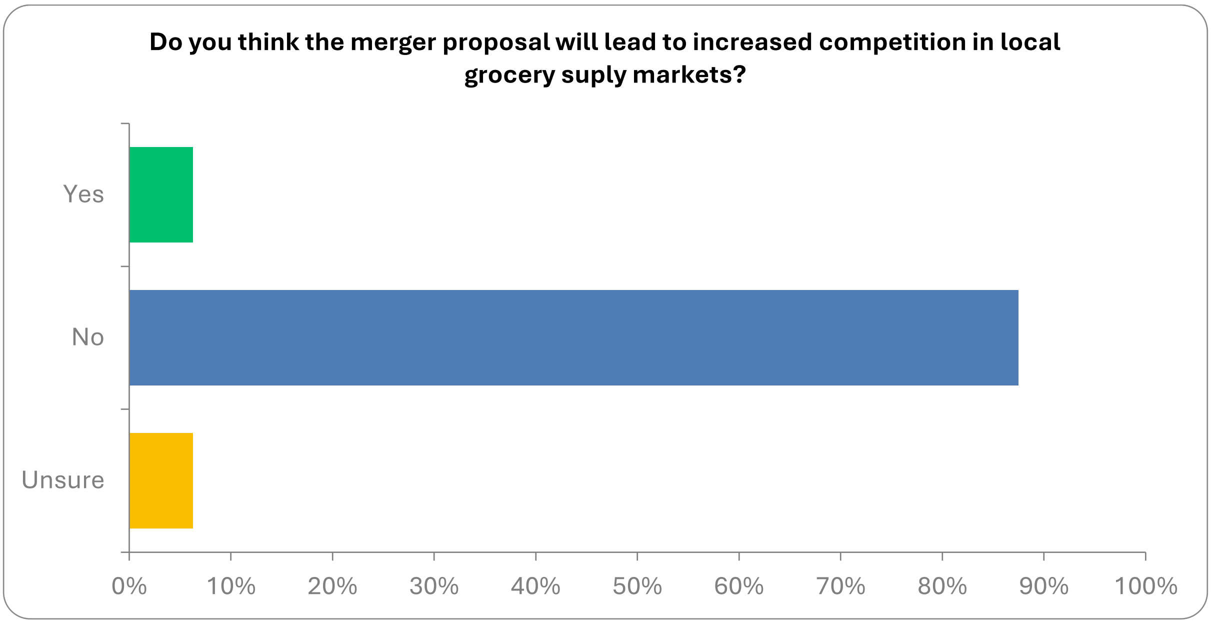
18.1 The SOI invites submissions and further information on whether the Proposed Merger would make any entry or expansion less likely.[73]

18.2 In the survey, 74% believed that the proposed merger would make it harder for new grocery retailers to enter. Further 87% did not believe that the merger proposal would lead to any increased of competition in local grocery supply markets.

18.3 Asking about the short to medium term because of the proposed merger, suppliers commented on the viability of New Zealand's market for global retailers. There is a prevailing sentiment that our small country may not attract significant investment from other parties. Concerns about timing also arise, with the current timeframe not appearing conducive to such endeavours.

18.4 However, amidst these considerations, there was a recognition of the impact from players like TWG and Costco, injecting some hope into the market landscape but not enough to temper concerns or belief there will be marked difference.

FIGURE 6.



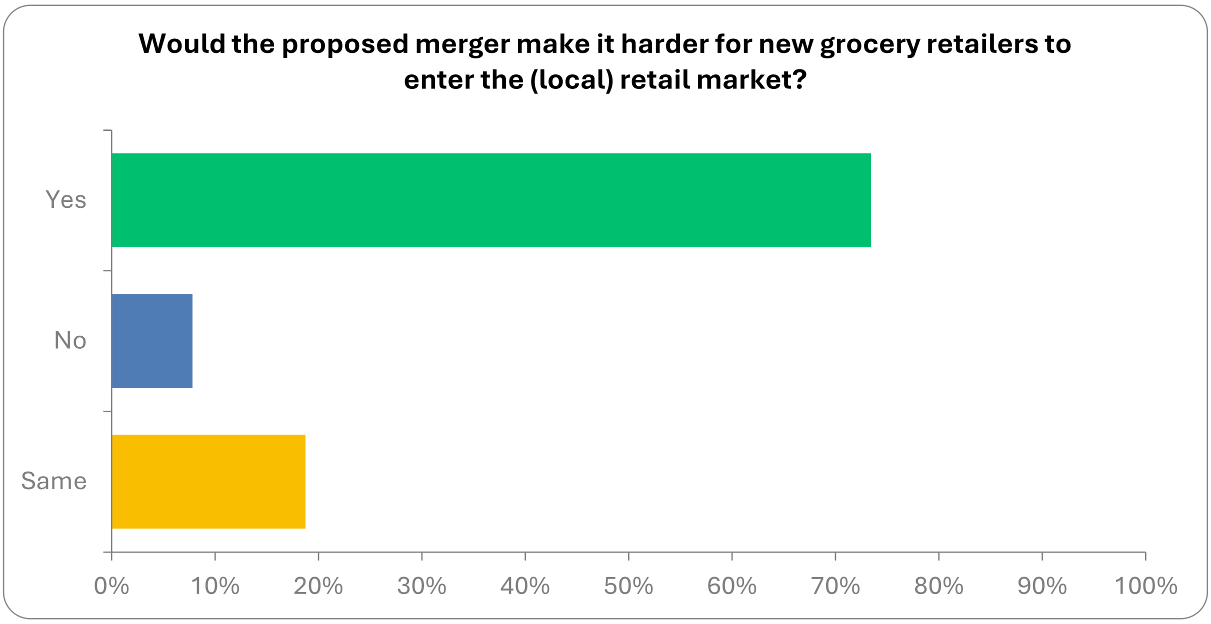
18.5 Despite the growing influx of new FS and WWNZ stores, outpacing other non-regulated retailers, the consensus is that substantial change may be slow to materialise over the next few years. This is attributed to the high barriers preventing new entrants from gaining a foothold, compounded by the dominance of existing players who have already secured prime locations.

18.6 Further considering the impending proposed merger and the potential market dominance of FS, strategies to safeguard business interests are being considered, with heightened

[73] Paragraph 162 SOI.

focus on mitigating risks associated with potential changes in product lines or market dynamics.

FIGURE 7.



18.7 Significant shifts in market dynamics are seen as contingent upon the entry of more large-scale retailers, while the prospect of competitor growth remains subdued, further hindered by the increasing market power of FS. Overall, the prevailing sentiment among stakeholders is one of cautious optimism tempered by the recognition of the formidable challenges inherent in competing within our market landscape.

i. The supplier believes that our small market size makes it unlikely for major investments from global retailers.

ii. The supplier does not expect much change as a result of the proposed merger.

iii. The supplier hopes that some competition from TWG and Costco could be positive.

iv. The supplier believes that the expansion of FS and WWNZ stores is ongoing, surpassing other non-regulated retailers.

v. The supplier anticipates minimal changes in the market over the next 1-5 years, with a possibility of a few additional Costco stores.

vi. The supplier believes that the entry barriers for new competitors remain high.

vii. The supplier believes that it is unlikely for new players to develop significantly due to the dominance of existing RGRs and their coverage of prime sites.

viii. The supplier suggested that they would prioritise actions to safeguard their business, considering the dominant position of FS in the market post-merger, concern about lines being deleted given they will be even more of a dominant market player.

ix. The supplier believed that there would need to be significant changes in the market that could then enable the entry of RGRs with substantial scale.

x. The supplier believed that any new competitor's growth would be slow, especially with the increasing market power of FS.