HABILIS

Submission: PBT Couriers acquisition by NZ Post

Response to Preliminary Issues Paper | 14 January 2024

HABILIS

Introduction

He tina ki runga, he tāmore ki raro.

In order to flourish above, one must be firmly rooted below.

This submission is made in response to the merger application made by NZ Post to acquire the courier business of PBT Group. We are opposed to the merger on the grounds that it will significantly lessen competition for courier services in Aotearoa, consolidate the industry further with a high likelihood of adverse market outcomes for customers, and increase the barriers to entry for new competitors.

We also take issue with the Commission's management of the process, particularly the over-reliance on the representations of the acquiring party (NZ Post), the lack of independent analysis of the market and its functioning before seeking public submissions, and on the invidious timelines that have resulted in the public being asked to provide input on a technically complex matter in the weeks immediately preceding Christmas, with only a two week window. In our view this represents bad faith by the Commission in its interactions with the public.

Our document is therefore in two sections:

1. **Issues about the process** deals with the Commission's failure to provide sufficient information or time for interested parties to provide an informed submissions
2. **The substantive matter** of the acquisition itself, which will result in adverse market outcomes if approved.

We ask that the Commission declines the merger application on the grounds that it will significantly lessen competition in the regional courier market; however, we note that the Commission has not declined a single merger application since 2018, bringing into question how it is managing to correctly discharge its regulatory responsibilities.

About us

Habilis New Zealand Ltd provides consultancy and advisory services to regional Aotearoa, including strategy development, economic and social impact modelling, business case and investment proposal development, stakeholder engagement and communications, and benefit and impact analysis. Our client base includes iwi, NGOs, local government and the private sector.

Habilis NZ Ltd is based in Tāmaki Makaurau.

Issues about the process

On 7 December 2023 the Commission released a Preliminary Issues Paper on the proposed acquisition of the courier business of PBT Group by NZ Post. The Commission invited submissions from all interested parties.

The timeline issues

As noted in the introduction, expecting interested parties to provide any sort of considered submission on a proposed merger that will have national implications within a two week window is unhelpful at best. As the merger application notes, the courier business covers the length and breadth of Aotearoa, so there may well be interested parties whose assessment of the impact will take some time given the nature and extent of the potential impacts.

And to schedule the consultation window for the two weeks leading up to the Christmas break is reprehensible behaviour from the Commission. For most people in most private sector businesses, this is the busiest time of the year – and this is doubly true of the very companies that are the customers of courier services. To expect these businesses to take time out of what may well be the part of the year when they generate a significant proportion of their annual revenue is simply unreasonable.

This is a repetition of the systemic failings in the Commission's engagement model. For whatever reason, the Commission seems to assume the private sector is willing and able to drop whatever it is doing to provide input to the Commission in major matters; the Commission has done this time and time again. There seems to be a Wellington bureaucratic conceit that the timelines of whatever process agencies are currently running will be the most important agenda item for every organisation and individual in the country.

Yet in comparison, the Commission allows itself much longer timelines to provide information or conduct analysis.

For instance, the Commission's Merger Assessment Guidelines (MAGs) note in paragraph 6.26 (page 40), the SOPI is due for release some 5 working days after the application is received. As the documents show, the application from NZ Post was received on 20 November 2023, yet the SOPI was not released until 7 December 2023, some 13 working days later.

It's this delay from the Commission that has resulted in the submission period being squeezed against the Christmas shutdown period, not the requirements of legislation *per se*. Had the Commission completed its work in a timely manner – rather than taking nearly three times longer than specified in its own process documentation – then the issue may have been less pressing for all interested parties.

In another example, the Commission provided its usual short windows for the recent merger application by Sealord Group/Independent Fisheries, and expected industry and iwi to respond with alacrity; yet a month after the clearance was approved, the Commission's final report is still missing in action.

It's deeply disappointing that the Commission thinks it is the only organisation that should enjoy the luxury of reasonable deadlines.

The analysis shortfall

It's also disappointing that the Commission's supporting material for making an informed submission is woefully inadequate.

We note that the Preliminary Issues Paper is largely composed of elements copied and pasted from NZ Post's clearance application, using what is clearly a standard template for PIPs. As a result, there is insufficient information for interested parties to be able to make a cogent submission. The dearth of useful analysis is in the following areas:

1. There is no definition of the market, other than that provided by NZ Post itself. As such, it is exceptionally difficult for submitters to be clear about the implications of the merger, and this runs the risk that the Commission's *post facto* definition of the market will entirely discount the views of submitters because we are talking about different markets. This is directly prejudicial to interested parties.

2. There is no information provided about the market shares or strengths of any of the market participants. The information in the PIP seems entirely copied and pasted from the NZ Post application, with no subsequent analysis or validation. What statistical information is available in the NZ Post application has been redacted, so is unavailable to submitters. As such, interested parties have no way of knowing what the relative market power of participants is, or - in the case of the PIP - even how many minor participants there might be. The Commission's approach to information provision is shoddy and lazy.

Further, there has been no attempt by the Commission to address any of the equity issues inherent in its process. NZ Post has obviously had many months to prepare the application and has the financial wherewithal to engage some of the country's best legal and consulting firms to do so. In comparison, other interested parties are being given a mere two weeks to make a fulsome submission – and even if they have the financial resources to engage similarly qualified professional assistance, the odds of being able to obtain the necessary personnel in the two weeks before Christmas is basically zero. This is highly prejudicial to the public interest.

As is the case with practically every other submission process run by the Commission, the major market participants are being granted the time and resource to make thorough and well reasoned arguments, whilst all other market participants and the general public – who will inevitably pay the costs of anti-competitive mergers – are being restricted to short windows and inadequate information. Given this happens time and time again, we can only conclude it is the direct, intentional policy of the Commission.

The likelihood of poor outcomes

As is clear from the way the Commission is running the submission process, it is merely consultation theatre – that is, it provides the illusion that consultation has occurred, whilst erecting every conceivable obstacle to meaningful engagement with parties other than the applicant. The purpose of the process is clearly to enable officials to tick a compliance box, whilst not burdening themselves with too much work.

This cynical bureaucratic approach has led to invidious outcomes for Aotearoa. We note from the Commission's case register that no merger application has been declined since 2018, indicating the process is merely a compliance way-point with no believable likelihood that regulatory intervention will occur. We strongly suspect the Commission has begun measuring its KPIs by the number of merger applications successfully approved, rather than by whether there are vibrant and effectively operating markets for goods and services in Aotearoa; in other words, the Commission's only goal is process efficiency, not societal outcomes.

And as a result of the Commission's inaction to prevent excessive market consolidation, oligarchies have formed. These include the banking sector, the supermarket sector, the electricity sector, the building products sector, and more. In every case, there are a small number of outsized participants engaging in the systematic abuse of market power, to the detriment of the country.

As the Commission's own market studies show, these oligarchies are levying super-profits at the expense of consumers, to the tune of many billions of dollars a year. And as many of the participants are overseas owned, the excessive profits are imposing a further deadweight drag on Aotearoa's economy, to the detriment of whānau, businesses, farms, and our wider national wellbeing.

Unfortunately, the Commission has been entirely remiss at addressing these oligarchic behaviours, even though it has the legislative tools, the political mandate and the moral obligation to do so. The Commission has taken no legal action to break up any oligarchy since 2012, and it seems simply unbelievable that there has not been a single instance of the abuse of market power in that period. Yet despite the clear and obvious evidence of unjust enrichment at an industrial scale in vital markets, the Commission seems determined to never trouble the courts.

In fact, as the case register demonstrates, the Commission has been the primary architect of the undue consolidation and the resulting market abuses. The mergers in the banking sector that have led to the Australian banks holding >85% market share were approved by the Commission; ditto the consolidation in the supermarket sector; ditto the horizontal and vertical integration in the building products sector. The formation of oligarchies has not been an accident; the Commission has been an enthusiastic and willing midwife throughout the process.

For example, the Commission conducted a market study into building supplies, which concluded in December 2022. It stated that there are failures in the market – yet during the course of the study, the Commission approved the acquisition of Tumu ITM by Fletcher Distribution, thus increasing the vertical integration in the very sector under investigation.

Even when the Commission – in response to public concern and political direction – undertakes a study into a failing market, it is still prepared to rubber stamp every application that comes through the door, even when doing so will increase the very failure at the heart of the investigation.

Summary

It is therefore apparent that the country can have little faith in the actions of the Commission, because:

1. The time window for providing submissions is too short, and in the case of the PBT/NZ Post acquisition is deliberately being conducted in the weeks immediately preceding Christmas, prejudicing the participation of all other interested parties.

2. The information supplied by the Commission to enable other market participants and the wider public to make an informed submission is woefully inadequate.

3. Even if interested parties navigate the inherent inequities in the Commission's processes, its track record indicates that approval for the merger will be given in 100% of cases, irrespective of the subsequent adverse outcomes.

4. The Commission's track record also indicates that it will never take action to break up the oligarchies that form as a result of the mergers, nor to punish the unjust enrichment of participants that results.

It is therefore evident that the Commission is failing Aotearoa in the area of competition policy and enforcement.

Executive summary

The NZ Post asserts that the acquisition of the PBT courier business would not result in a significant lessening of competition in the national courier market. We disagree with this assessment, on the following grounds:

1. NZ Post has mis-characterised the nature of the courier market and the dynamics that give rise to scale effects and the resultant profitability of the larger operators. If the market is correctly characterised, then it becomes evident that the market does not function as NZ Post asserts.

2. As a result, NZ Post has mis-characterised the barriers to entry that exist for smaller operators, particularly those that are seeking to grow beyond a regional or market niche. These barriers are high – and growing higher over time – so the consolidation of courier companies through this acquisition risks creating yet another market oligopoly, with a small number of large operators able to generate super-profits at the expense of consumers, with little effective competition to constrain them.

We will address each of these issues in turn.

NZ Post's definition of the market

In its application, NZ Post describes the market as follows:

> 44. NZ Post submits that the relevant market is the national market for the provision of domestic courier services (the courier services market). The courier services market involves the pickup and delivery of ambient parcels under 25kg in weight.
>
> 45. Alternatively, NZ Post submits that the relevant markets are the national markets for the provision of domestic courier services to business for delivery to:
>
> > 45.1 other business customers (the B2B courier market) market; and
> >
> > 45.2 consumers (the B2C courier market).

This statement inverts the market dynamics, because it fails to describe the true nature of the market, which is shaped by network effects. NZ Post has merely described the market it wishes to address, not the market for services as expressed by customers for courier services.

If NZ Post's definition of the market is accepted, then the Commission runs the risk of excluding sectors of the market from its assessment where the effects of the proposed acquisition will be substantially negative. Accepting NZ Post's definition will substantially tilt the playing field in favour of the acquisition, to the detriment of the wider market.

And notably, NZ Post's application also fails to identify the factors that would lead to success or failure in the courier market, which is central to the issue of whether or not the acquisition will have a substantial negative effect on competition.

The dimensions of the courier market

As is clear from the academic literature, markets are not defined by what suppliers wish to provide; they are defined by what purchasers wish to procure. However, NZ Post has only identified some of the dimensions of the market as defined by purchasers, and as noted above this will have the effect of distorting the assessment process.

The real-world dimensions of the courier market are defined as follows:

1. The spatial distribution of pickup and delivery points across Aotearoa, with pickup and delivery to every location in the country

2. The temporal spread of how quickly items can be picked up and delivered, ranging from urgent deliveries through to extended delivery times as required for logistical or price reasons

3. The physical sizes and weights of the parcels being handled by the courier service, stretching from very small and light items all the way beyond the arbitrary 25kg limit set by NZ Post.

Within these three dimensions there are a wide range of services that purchasers wish to procure. There are wide extremes in every dimension, and the dimensions themselves are not coupled; that is, constraining one dimension does not automatically result in constraining any other dimension.

If we look at the range of values (services) in each dimension, they can encompass:

1. Spatially – pickup from and delivery to every single address in Aotearoa, from individual farmhouses in remote regions through to CBD offices and major business locations in our largest cities

2. Temporally – as soon as possible (less than one hour) delivery of urgent items through to best-efforts or significantly delayed delivery for items where there is no urgency, or when there is a business or personal gain to be enjoyed from slow delivery

3. Physically – items of trivial size and weight, such as individual documents, through to large, heavy or awkwardly shaped items that may require machinery to collect or deliver safely.

As can be seen, there is negligible coupling between the dimensions; a heavy and awkward item may be needed urgently, while a single small photograph can be delivered over many weeks; and all items have the potential to be collected from and delivered to any location.

Obviously, not all courier companies will provide services covering 100% of all three dimensions; however, it's safe to say that market demand exists at practically every point on the continuum of every dimension. This leads us to the important first principle of how the Commission needs to assess the application:

Principle 1:

The market for courier services is defined by what customers wish to purchase, not the subset of the market that NZ Post wishes to serve.

This is a vitally important principle: no single company defines the extent of the market. If they do so, then there is no open market for the goods or services they wish to provide. This leads us to our first recommendation:

Recommendation 1:

For the purposes of assessing the impact of the proposed acquisition, the Commission should define the market as the full range of courier services in Aotearoa as demanded by customers.

The complexity issue

As can be seen, these three dimensions – leaving aside the key issue of price – give rise to a very considerable level of complexity. Dealing with a large number of parcels with a large number of pickup and drop-off points across the country, some urgent and some not, and in a range of sizes and weights, inevitably leads to the requirement for a very high level of logistical management.

The primary way that courier companies attempt to manage the spiralling complexity demanded by the market is by constraining one or more (and in practice, all three) dimensions; they only provide services for a subset of the market, and practice active market and customer segmentation.

For instance, courier companies will typically set spatial constraints by specifying the area of the country or the types of locations they will pick up from or drop off to; they will only provide some temporal services, by excluding some options such as high-urgency deliveries; and they will put restrictions on parcel size, weight, dimensions or require that items fit standardised boxes or outers.

The effect of this constraint-through-segmentation can be shown diagrammatically, where a courier company will apply the constraints it thinks are in it best business interests in order to profitably serve a defined segment of the market:

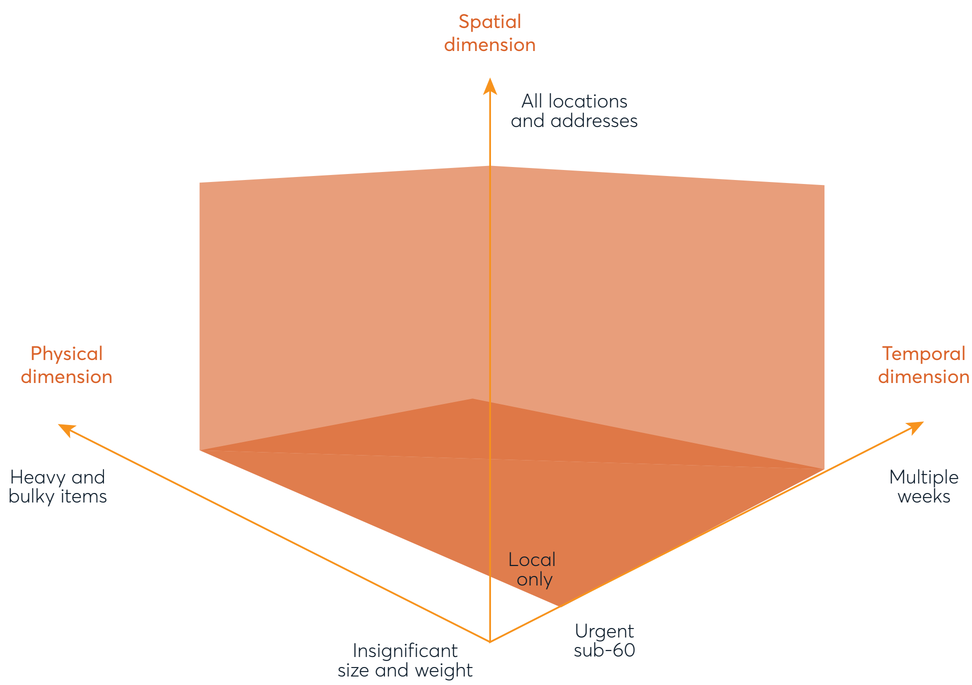

Figure 1: Market segmentation.

The orange bounding box defines the part of the market – with physical, temporal and spatial dimensions – each courier company wishes to service. The reason for constraining the complexity of the market is to manage the logistical difficulty of providing all services to all customers, whilst still making a profit.

Modelling complex networks

The inherent complexity within a courier network falls into a particular class of mathematical problems, known as NP-Hard. These are combinatorial optimization challenges, the aim of which is to optimise for the most efficient way of getting a parcel from its point of origin to its point of delivery, with a large number of variables – travel times, sorting times, traffic densities, van sizes, driver shifts, and many more – along the way.

The NP-Hard challenge that most people are familiar with is known as the "travelling salesman problem". This is a real-world optimisation problem, where the aim is to provide the most efficient way for a putative salesman to travel between customers in different cities, given the constraints of public and private transport. The travelling salesman problem – in both specific and generalised forms – is used extensively in logistical planning, in a wide variety of industries.

NP-Hard problems are exactly what they say on the tin: they're hard. As the Wikipedia article (a good starting point for the non-mathematical amongst us) notes:

> In the theory of computational complexity, the decision version of the Traveling Salesman Problem belongs to the class of NP-complete problems. Thus, it is possible that the worst-case running time for any algorithm for the Traveling Salesman Problem increases superpolynomially (but no more than exponentially) with the number of cities.

This is an expensive way of saying that the complexity of the travelling salesman problem grows very quickly, so our ability to efficiently solve the routing problems decreases rapidly as we add more variables – such as spatial, temporal or physical – to the equations.

If a single courier business was to provide services for 100% of the market in each of the dimensions, then the routing problems for the millions of parcels of widely divergent addresses, sizes and delivery times would become intractably difficult. This is at the heart of why courier businesses practice reasonably aggressive market and customer segmentation.

To illustrate the idea further, the core issue for the travelling salesman problem is that it must be solved for every single salesman if efficiencies are to be realised. Producing a single solution for a single salesman is no guarantee that the next solution – faced with a different mix of timetables, constraints, and customer requirements – will be in any way made easier. Each separate route needs to be calculated and optimised individually.

At the level of a courier business, then, the NP-Hard routing problem needs to be solved for every single parcel in the network, and then implemented logistically. This is both difficult and expensive, and is one of the reasons why scale doesn't always help when it comes to courier and freight companies; the complexity of the routing can grow faster than the financial returns from delivering packages.

In the context of the courier business in Aotearoa, then, the overwhelming drive for companies is to restrict the number of variables; in other words, to limit the number of locations, the range of delivery times, or the shape and weight of parcels, so that their operational logistics can be optimised as much as possible. Obviously, the larger the number of variables, the more complex the logistics, and the higher the costs. Too much service complexity can thoroughly destroy company profitability. This dynamic is as true of small courier companies – PBT Couriers – as it is of large ones, such as NZ Post.

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Principle 2:

The primary driver for profitability in the courier market is the ability of a company to solve network efficiency problems of the NP-Hard type.

> **Recommendation 2:**
>
> **For the purposes of assessing the impact of the proposed acquisition, the Commission should recognise that the courier market is primarily driven by network efficiency effects.**

The importance of computational competence

NP-Hard problems require significant knowledge of the inputs and considerable computational resource to solve, or to provide an approximation of a solution. As a result, they have been a focus of both the theoretical end and the practical software end of the IT industry for many decades. In areas as divergent as airline scheduling and TCP/IP packet routing, NP-Hard algorithms play a key role in trying to wring financial efficiencies out of complex networks with high capital and operating costs.

As is the case with courier companies, most networks are modelled using systems dynamics tools. This is a well-trodden path that models a complex system as a set of nested sub-systems, using stocks, flows, delays, feedback loops and a range of other components to simulate the flow of activity (or items) through a complex network. Obviously, the more complex the overall network, the greater the number of sub-systems, the greater the number of variables, and the greater the analytical and computing resources that must be brought to bear on the challenge.

An understanding of the real-world constraints and the effective modelling of how the sub-systems interact and interoperate is critically important to the profitability of any company that operates a complex logistical network. Understanding the constraints and bottlenecks allows changes to be made in operational procedures, which in turn have large impacts on the profitability or otherwise of both the sub-systems and the overall company.

The purpose of systems dynamics analysis – whether conducted in expensive IT systems for a large company, or calculated on the back of an envelope for a small one – is to translate insights about how the network is running into optimisation decisions that lead to greater profitability. This is the central driver for how effective any competitor will be in a market primarily driven by network effects. This dynamic is why NZ Post has made such a feature of its network investments in its application:

> 35. NZ Post has invested over $200m in its Te Iho network transformation programme. Te Iho is a strategic, long-term investment that involves development of an automated national parcel processing network. For example:
>
> > 35.1 in August 2022, NZ Post opened the Christchurch Processing Centre, which added new automation to its existing Southern Operations Centre, and is designed to process 17,000 parcels per hour;
> >
> > 35.2 in October 2022, NZ Post opened its new Wellington Depot, its first automated parcel processing hub in the lower North Island, designed to process up to 11,000 parcels per hour; and
> >
> > 35.3 the new Auckland Processing Centre is due to open in the first half of 2024.

In our view, this is all slightly misleading. While the processing centres are undoubtedly important, they are merely an operational manifestation of the investment into systems dynamics analysis – undoubtedly supported by the IT analytical tools and operational systems required for improved modelling and implementation.

The value of a courier network – and therefore the courier business – depends, therefore, on the level of optimisation that has been achieved, because this is strongly linked to its financial performance.

For instance, two courier companies may target an identical market segment, have identical logistical capabilities, and invest the same amount of capital in buildings and systems and machinery. However, the level of profitability of the two businesses will not primarily depend on these factors; it will be driven by the level of optimisation (and therefore efficiency) obtained by each company.

If Company #1's network is poorly optimised compared to Company #2, it will have higher costs and lower profitability. The constraining factor is not the number of courier vans or distribution centres, but the investment in understanding, modelling and optimising the use of those resources to deliver parcels at the lowest cost per unit.

Barriers to entry in the courier market

On the surface, anyone can start a courier company – vans and warehouses are comparatively cheap. Yet most courier businesses are small, have difficulty growing beyond a specific market or geographic niche, and routinely fail. This is not because the people running them lack the skills to operate a courier company; it is primarily because they lack the skill to analyse, understand and optimise the systems dynamics that shape their business.

As is the case in most other sectors, new small entrants tend to be individuals who understand the operational nature of their sector; as an example, new plumbing companies are predominantly started by plumbers, who have the domain expertise to install and fix pipes.

However, the success or failure of the business generally depends on factors that have nothing to do with domain expertise in a specific sector. These include skills in attracting, hiring and managing staff, raising and making good use of capital, understanding the competitive environment and constructing differentiated products and services, and much more.

And so it goes with the courier market, with the notable exception of requiring skills in complex network optimisation. Unlike – say – basic HR practices or health and safety fundamentals, these skills are not easily or cheaply available, even when the requirement for them is identified. But without those skills, the networks and processes constructed by entrant courier companies will be sub-optimal, less profitable, and they will be able to be easily out-competed by more sophisticated operators.

In essence, then, the courier vans and warehousing space contained within NZ Post's Te Iho investment are merely the basic operating requirements of any courier business, and don't possess any intrinsic strategic value on their own; it's the investment in modelling and optimisation that does. It's the knowledge and analysis enshrined in the IT systems that contains the key to NZ Post's future profitability.

And herein lies the challenge for any new market entrant. The barriers to entry are very significant indeed, despite NZ Post's rhetoric to the contrary:

> 114. However, if prices rose above, or service levels fell below, competitive levels, then market entry could be expected. Conditions of entry in these markets are benign with the services provided able to be replicated by anyone with modest levels of investment. That would certainly be true for an entrant seeking to replicate PBT's market position.

As we have shown, the barrier to entry in the courier market is not the purchase of courier vans and warehousing space; it's the knowledge of and investment in the modelling and optimisation of the complex flow of logistics through the network. Without this understanding – and the necessary investment in implementing the required optimisations – then there is no believable mechanism for a new major competitor to arise.

Principle 3:

Barriers to entry are created and sustained by the ability to solve NP-Hard routing and efficiency problems in real time, which requires significant knowledge and computational expertise.

> **Recommendation 2:**
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> **For the purposes of assessing the impact of the proposed acquisition, the Commission should recognise that the barriers to entry to the market are knowledge and computational expertise, not access to capital or physical resources.**

The fractal nature of the sector

It is entirely clear from NZ Post's application discussing the competitive landscape that the courier sector is fractal in nature; that is, it exhibits the same degree of complexity at every level of scale.

NZ Post identifies Freightways and Aramex as the major competitors in the market, then lists a number of medium-sized businesses – including PBT couriers – as the next tier down, followed by a recognition of unnamed minor players. This reflects the core market dynamic, where no company other than the majors has the resources to invest in the modelling and network optimisation to grow to national scale.

NZ Post state this in their application:

> 37. PBT threw everything it could into its courier business over the last 30 years. However, PBT has decided to "de-verticalise" and focus on its core freight and logistics businesses. With those businesses being where PBT started; and where it now makes sense for PBT to return.
>
> 38. At the business-to-business focussed market segment, where PBT has found a minor place in the courier industry, PBT faces intense competition from many other small courier companies [PBT Confidential].

In effect, PBT couriers are saying that they have been unable to achieve the network optimisations of their larger competitors, which has resulted in lower levels of profit than shareholders expect. This could be for a range of reasons, such as the strategic focus of the company group being elsewhere, external capital constraints, competition from more profitable parts of the company group for limited capital, the high cost and complexity of obtaining suitably talented staff, and many others. In that sense, exiting from the courier business is clearly a good decision for PBT Group and its shareholders.

And it seems highly likely that PBT Group has killed and experienced governance and management, with considerable depth of expertise in the logistics that are at the heart of the freight and courier businesses. Yet even so, the necessary network optimisations that its major competitors – NZ Post, Freightways and Aramex – have achieved are unable to be realised by a skilled organisation with decades of successful track record.

In this context, NZ Post's assertion in its application that the barriers to entry for new competitors are low seems somewhat disingenuous. It hardly seems likely that both things can be true at the same time – that the highly experienced PBT Group is unable to sustain a profitable courier business, and that new entrants can magically be expected to spontaneously arise if prices increase.

Based on the size and complexity of the courier market in Aotearoa – as defined by customer desire rather than NZ Post's preferences – we will go so far as to say that there will be no major new entrants to the market offering a similar range of services. This is because a new entrant will need the knowledge and data already in the possession of the three major companies in order to optimise their network and therefore be able to compete on price and service. There are few believable paths to this occurring, as the PBT couriers experience has shown.

The significant risks of oligopoly

The requirement for an in-depth understanding of network logistics in Aotearoa constraints the source of new competitors to the market. Any new major competitors to the entrenched tri-opoly are therefore likely to come from the current mid-sized operators, who possess at least a portion of the knowledge and experience to sustain and optimise a national courier network.

There are obviously a number of routes for a major competitor to develop from the current pool of mid-size players, including mergers and consolidation, organic growth, or external drivers such as acquisitions by companies in adjacent markets. We have no view about how or when or if this will occur.

However, it is abundantly clear that allowing the major companies – NZ Post, Freightways and Aramex - to acquire mid-sized courier businesses will materially reduce the opportunity for any mid-tier growth or consolidation to occur, which will decrease the level of competition in the courier market.

As we have established, the barriers to entry are high, as they are underpinned by sufficient knowledge of logistics in Aotearoa and the necessary resources to model and optimise the courier network. By allowing the largest companies to effectively poach the skills and expertise from the mid market, the number of companies that could believably grow into a national competitor will decrease. This is not in the best interests of consumers and runs the risk of market failure.

The Commission has not made any information about the relative market shares of the major or mid-tier companies available, nor is there any believable way for us to obtain the data in the short submission window in the middle of the summer holidays. However, Aotearoa's experience of market failure in a range of sectors is worth noting:

- The banking sector is exhibiting strong evidence of market failure with four major Australian banks forming an oligopoly, as evidenced by excessive profitability, negligible customer churn, the wholesale transfer of risk from banks to customers, high barriers to entry, and a failure of the major banks to innovate.

- The **grocery sector** is also exhibiting the features of market failure and oligopoly with the actions of two major companies. This is also evidenced by excessive returns on capital and unjust enrichment, insurmountable barriers to entry, reduced consumer choice, and negligible innovation for consumers.

We won't over-labour the point by continuing to list other sectors, but clearly the country has a problem with over-much consolidation leading to anti-competitive behaviour from dominant market players. However, it is worth noting that all of these oligopolies were allowed to form because the Commission approved excess consolidation in the relevant sectors.

In this context, the NZ Post application seems to highlight exactly the same trend:

> 36. Given these investments, NZ Post's rationale is simply that it sees the acquisition as a way to add volume to its existing courier business without materially increasing its costs. As a result, NZ Post expects to achieve greater cost and customer service efficiencies in the delivery of courier services, enabling it to compete even more effectively with Freightways, in particular, and others.

Principle 4:

The high barriers to entry mean that there is a significant risk of an oligopoly developing between the three major companies, with adverse effects on consumers and the wider economy.

> **Recommendation 4:**
>
> **For the purposes of assessing the impact of the proposed acquisition, the Commission should recognise the risk of oligopoly formation and its adverse effects.**

Impacts on customers

It is clear from the application and from the product information on the respective companies websites that there is an imperfect overlap of products between NZ Post and PBT Courier, particularly when viewed from a customer perspective. PBT Couriers only provide services to a subset of the possible market demand, and NZ Post provides a similar but not completely overlapping subset of services to the possible market demand.

This makes sense: both companies have made different optimisation decisions about which segments of the available market they wish to service, based on their logistical capabilities. As we have noted, the profit imperative provide a strong incentive for all courier companies to size and shape their operations to ensure they can provide their courier services in the most efficient way possible. That trend lies at the heart of the parties' reason for undertaking this transaction.

It is reasonable to assume that the acquisition will not materially alter NZ Post's optimisation decisions. In practice, this indicates NZ Post will cease offering products and services that aren't aligned with its current logistical arrangements.

Notably, in its application NZ Post does not describe what will happen to the services currently provided by PBT Couriers that are not currently provided by NZ Post, and which they have no intention of providing in the future. NZ Post has not quantified the size of this market, or the impact on purchasers from the ending of provision. These effects may be more than minor, particularly for businesses where the delivery of non-standard items is a key component of their operations.

The potential impact is shown by the early concerns raised by submitters who are routinely using PBT Couriers services. For instance, some of the early submitters raise concerns about the loss of services for irregularly shaped packages, or those of more than 25kg. While NZ Post declaims these requirements and states they are outside the defined market, it is entirely clear that purchasers wish to procure them. NZ Post discontinuing the provision of these services will unequivocally have a negative impact on market choice for some consumers, and result in less competition for that subset of products compared to the status quo.

The submissions also highlight that there are efficiencies for some businesses in having a single suppler for both courier parcels and more general freight items, which is currently filled by PBT. These efficiencies will cease if the acquisition is approved, and the additional costs will be borne by customers compared to the status quo. In effect, this partial cost of the transaction and its consequences will be externalised to customers.

Principle 5:

The consolidation of market share in the hands of NZ Post will see a reduction in product and service choice, driven by NZ Post's desire for efficiency and profit gains as a result of the transaction.

> **Recommendation 2:**
>
> **For the purposes of assessing the impact of the proposed acquisition, the Commission should recognise that there will be material adverse effects on some parts of the courier services market, and efficiency losses to those consumers.**

Allocation of benefits

There are significant dis-benefits to consumers in this transaction, for the following reasons:

- The available choices for courier services will decline once PBT Couriers is assimilated into NZ Post, so there will be less competition for customers.
- There will be efficiency losses for some customers as NZ Post withdraws from providing PBT Couriers products and services they no longer wish to support, forcing these customers to deal with multiple providers.
- There is a material risk of an oligopoly forming in the courier market due to a small number of large companies having excessive market share and being able to dictate prices, as has happened in banking, supermarkets and a range of other sector.
- As the barrier to entry for national-scale competitors are very high, there is a reduced chance that a new major courier company will arise if consolidation of the sector is approved by the Commission, compared to the status quo.

There are material benefits to NZ Post from the transaction, as follows:

- The logistical and operational knowledge contained within the PBT Couriers business will be of benefit to NZ Post in the further optimisation of its network, which should result in higher efficiencies and higher profits.

- There may be some logistical economies of scale at NZ Post's centralised facilities, although we remain sceptical about the significance of these given the strong network effects within the courier business.
- There is a benefit in acquiring PBT Courier's customer base, with potential lock-in effects if geography or business type constrain the available choices for certain customers, and there may be the opportunity to obtain higher margins from these customers.

There are material benefits to PBT Couriers from the transaction, as follows:

- The company will be able to reallocate capital to other aspects of Group operations, to the benefit of shareholders.
- The Group will also be able to redirect governance and management time and focus into areas that are more aligned with its long-term strategic direction, to the benefit of the company and its shareholders.

In summary

Selling the PBT Couriers business clearly makes sense for PBT Group shareholders, and there is likely to be a capital and economic efficiency argument that supports the actions of the company in seeking a buyer; we are obviously not opposed to PBT Group divesting itself of the courier business.

We are, however, opposed to NZ Post – or, for that matter, Freightways or Aramex – being the buyer. The reasons are as follows:

1. There is already limited competition in the national courier market, with only three major companies competing. No other companies are likely to achieve the market reach or network efficiencies in the short term.

2. The nature of the network effects within any courier business mean that the barriers to entry are high, and there are severe efficiencies of scale in effect due to the knowledge and computing expertise needed to operate an efficient and profitable national business.

3. Allowing further consolidation of the industry into the hands of any of the three major incumbents would serve to raise the barriers to entry higher, which runs the risk of an oligopoly forming – as has been the case in the banking, supermarket, building supplies and electricity markets, amongst others.

4. Removing a mid-sized competitor – PBT Couriers – will act as an impediment to mergers and acquisitions between small and medium sized companies that may one day result in a viable competitor to the three major incumbents.

5. There is strong evidence of consumer harm from the transaction, as the range of products and services will decline as NZ Post abandons some of the offerings currently provided by PBT Couriers. Further, there will be efficiency losses to businesses as a result of the change in market offerings.

6. There is no evidence that the efficiency gains being touted by NZ Post will ever accrue to consumers. NZ Post make no statements about the level of efficiency gains expected, and no commitments that these gains will be passed onto consumers in any fashion.

In other words, the benefits of this transaction accrue solely to the shareholders of NZ Post and PBT Couriers, and the dis-benefits are felt solely by consumers in the courier market – both in the short term, with decreased competition and a more limited range of products, and in the medium term with the further consolidation to the point of potential oligopolic formation.

This transaction is not in the best interests of the country and should therefore be declined by the Commission.

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