



**PUBLIC VERSION**

## **LIFE HEALTH FOODS/CHALMBERS ORGANICS**

### **CHALMERS ORGANICS LIMITED SUBMISSION ON SoUI**

**17<sup>th</sup> May 2022**

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## SCOPE

This submission is provided to assist the Commerce Commission, in its consideration of the clearance application, lodged by Life Health Foods, to acquire Chalmers Organics.

We have noted that there are three main concerns discussed within the Commerce Commission's SoUI, they are: -

- a) Competitive constraints,
- b) Entry of New Suppliers
- c) Relevant Markets.

We further note that the Commerce Commission is now only specifically concerned with the area of Tofu. So will address this accordingly. We will also endeavour not to repeat what was previously sent in our last submission, except in terms of reference.

## COMPETITIVE CONSTRAINTS

The Commerce Commission states that tofu price increases and lack of competition, could be a result of the proposed acquisition.

We disagree, it is our view that the deciding factor of competitiveness in supermarkets is as follows: -

1. Supermarkets and consumers decide the price of products, as most consumers will not purchase highly priced products.
2. Supermarkets will not stock items that do not move quickly or give them their desired profit. They decide what they will stock by using this criterion. Our 25-year experience with supermarkets shows us that this is the actual deciding factor in price competitiveness.
3. Consumers would just buy their tofu elsewhere, as is possible with the market spread of tofu products, of which there are now so many.
4. We assert here that falling sales, as a result of high prices would trigger a deletion from supermarkets. This would then allow other tofu manufacturers to take up the slack. Tofu is only 0.06% of supermarket's turnover. (See table below)
5. We further note there are many vegetarian/vegan products, and vegetarian/vegan consumers are used to shopping elsewhere.
6. If supermarkets wanted to replace any brand of tofu, this would be easily achieved by facilitating the entry of new suppliers into their stores, the current barriers, to new suppliers, being mainly financial e.g., discounts, specials etc., that are all carried by the supplier. All food manufacturers in New Zealand have the same compliance costs no matter where they are selling their goods. All must have a food safety plan, and be registered as such.
7. We note that Asian manufacturers in particular produce extremely cheap tofu as evidenced in our previous submission. Brand replacement can also be achieved by buying from those currently supplying Asian stores; some of these overseas manufacturers are big corporations. Both supermarket chains also have in house brands and new tofu suppliers are constantly coming into the market. The merged entity could not control pricing where

supermarkets have house brands at very low prices and Asian suppliers offering tofu at even lower prices than that.

8. We suggest that supermarkets are not a “complete block” as suggested by the Commerce Commission, that would inhibit entry by small companies, e.g., Foodstuffs stores are individually owned and operate as such, Countdown stores and Fresh choice are equally separate from each other and the main block. Further to this these stores are managed by individual managers who have discretionary pricing and ranging abilities. We suggest this negotiating ability gives the supermarkets considerable strength and flexibility. For example, Chalmers Organics and Bean Supreme company histories demonstrated this, even Countdown stores will “test” new products and suppliers first by only ranging in a few stores to see how a product performs in consumer demand, rate of sale and profitability.
9. We maintain that contrary to what is suggested by the Commerce Commission, i.e., (that the emerged entity could have control over pricing) that no entity has ever been able to sell their products at an unjustifiable price. Also, suppliers are now required to submit a case for any price increases, providing evidence to show why prices need to increase. There is no longer opportunity for any supplier to increase prices beyond what relates directly to increased costs for those products.
10. Regarding competitive edge, if LHF artificially increased tofu prices, we suggest that it would only make it easier for new suppliers to enter the market, as consumers will generally switch to a cheaper brand e.g., Pams and Macro. Macro is the category leader. The merged entity could not increase prices as it would not be competitive with Macro.
11. The Commerce Commission has suggested that tofu is its own category and consumers will not interchange with other plant-based products. We dispute this because, [  
  
]. Consumers swap between the types of products and will eat less tofu if it becomes too expensive.

## ENTRY OF NEW SUPPLIERS

The Commerce Commission suggests that new suppliers will have difficulty competing with the merged entity. We suggest that it is the reverse.

1. **Simplicity** – ease of entry into the market. The tofu process is extremely simple and you can increase output by just using more labour e.g., extra shifts. Once you have established the market you can then upgrade your machinery and reduce labour. This is how we managed to keep up with demand and anyone else can do the same. We have done this in the past and indeed had to do this recently during the Covid period, when supermarket sales increased substantially, and have now gone back to normal, e.g., we had to put on a temporary night shift.
2. **Entry into supermarkets** The Commerce Commission implies that compliance costs may reduce entry for new suppliers into the market. We disagree, and suggest the following. It is important to note here Chalmers Organics only have a Food Control Plan, this is the basic

requirement required of all food manufactures or handlers in NZ. Meaning we have the same certification than all other manufactures of tofu in NZ. If you are handling Meat or Dairy the compliance is much higher. We have not been required to do more than existing tofu makers already have. It is important to dispel this, in case there still remains some indication that it is not possible to supply supermarkets without some change to the compliance status of their businesses. The **ONLY** constraint to supermarket entry is a financial one, not one of compliance. Any store/supermarket can waive this if they so desire and could thereby help new suppliers into the market. There are no other constraints.

3. The Commerce Commission have asked us to explain how we have been able to expand our supply of tofu to the major grocery retailers both in the past and more recently.

**a) How we started.** Until 3 years ago we have no automation at all and have functioned like that for 23 odd years through all our growth from a business, with just the 4 of us to a few years ago when we first moved to our new site expanding a team of 55.

**b) How we have been able to expand our supply of tofu to the major grocery retailers both in the past and more recently?**

Like most manufacturers, when we wish to grow or are presented with a business opportunity to supply more product, we have certain levers we can use to increase output. Our tofu room is manual and labour intensive. We have not yet invested in any automation This informs our view that as we have done historically, any small tofu manufacturer can grow their output with gradual and small investments. By adding more shifts thereby increasing the time you manufacture product and thereby increasing volume, you can wait until profit and cash allow incremental investment in process improvements that make processers more efficient and jobs less labour intensive. This is how most entrepreneurial companies grow here in New Zealand. Using little venture capital and high labour component cost as they expand and grow, using profit to pay for process and plant improvements.

Labour continues to be our largest cost to produce. This approach has given us flexibility and allowed us to dial production up and down and expand and reduce production levels as required, all without prohibitively high fixed overheads (e.g., debt servicing on capital investment). During the recent Covid 19 pandemic lockdown as our sales fluctuated up to record highs, we were able to increase shifts. When demand subsided, we then reduced back down again. Over the years we have slowly supplemented machinery into the tofu line, adding a new press or cooker to organically and slowly increase outputs, as funds allowed.

**c) What role the major grocery retailers have in our growth;**

Historically the supermarkets have allowed us to grow organically and gradually in the market. When we communicate clearly and well, they are happy to start ranging's slowly and carefully for any new products. All our products have varying ranging's across the stores and as new products are released to market, we have been able to request a small ranging if required to test and grow a product, before we commit to any significant capital investment. Historically and in Countdown especially we have tried, not always successfully, to negotiate larger initial ranging however, Countdown are keen to first test in a small number of stores, before extending a product ranging nationwide and

eventually perhaps to all stores. This has been our experience and is our view in the case of every product we have ever bought to market. This view based on experience precludes a theory that LHF would be able to have lasting and significant control over both chains of supermarkets due to supplying the bulk of tofu. Both chains of supermarkets are still capable of recruiting and supporting existing smaller suppliers to enter the market gradually, and likewise reduce LHF ranging's to compensate and support new suppliers.

4. The Commerce Commission suggested that the amalgamation with LHF will block small suppliers entering the market. We disagree with this because when we entered the tofu market Bean Supreme was the sole tofu supplier in the supermarkets, with total dominance over tofu supply. They were a much larger and well-resourced and had an established brand and business. We entered the market slowly supplying first our own Health Food store in Glen Eden and building to all Health foods stores nationwide, and then slowly spreading into supermarkets in Auckland and then across the country.

## RELEVANT MARKETS

The commerce Commission suggests that tofu cannot be substituted and is therefore its own category. Therefore, the proposed entity will have an advantage because of lack of competition, it will be too dominant in the category.

1. As mentioned, the Commerce Commission has rightly stated, tofu is primarily an Asian food. Consequently, greater quantities are sold in Asian supermarkets under many different types. However, the commerce commission has considered this type of consumer outlet to not be of relevance in its investigations, and is now solely concerned with the two supermarket chains. We still strongly assert that the Asian supermarkets are part of the retail tofu market and in fact are the leaders, inventors and innovators. However, as previously pointed out, Asian tofu manufacturers are slowly entering into the supermarkets with tofu products. Meaning they are in fact able to enter into supermarkets and will grow sales. Therefore, will provide competition to the proposed merger. In the two predominant supermarket chains, basically, there is only firm tofu and even firmer tofu. This is because it is mainly non-Asian consumers buying tofu here. However, more Asian suppliers are entering with their products as more Asian New Zealanders demand their presence there.
2. Tofu is not a standalone category for our customers who are mainly vegan/vegetarian/flexitarian. They see our tofu as just one option for their protein requirements, and they use many different protein options e.g., vegetarian sausages/patties/meals/etc., but not lots of different tofu styles as found in Asian supermarkets. At the most, they would probably only eat tofu once a week. This is confirmed by the relatively trivial amounts of tofu that is bought in the two western chains when compared to Asian supermarket sales (please see previous submission). In conclusion this means that tofu is interchangeable with other protein options and is therefore not a stand-alone category.

3. Tofu is placed in the chilled vegetarian category where it is used as part of the vegetarians / vegan general meal options, not as a staple like in Asian stores where tofu is added to many dishes as a staple food source. This is independently evidenced in the data we receive from A.C. Nielsen.

## IN CONCLUSION

Chalmers Organics is a small family business owned and operated by the Chalmers Family, and is a culmination of previous businesses that have bought it to this point in time. Our impulse for starting this type of business was to provide truly healthy food for both people and the planet. Profit has always been needed (in order to grow and survive) but was in no way the primary purpose. We have paid a Living Wage for many years now, and this has meant less profit (but still sufficient for growth). As such we have slowly grown the business over the last few years, and have come to a place where, in order to meet the market, we need to substantially expand.

We see that the acquisition by LHF will allow for this growth. We have worked hard to ensure this acquisition actually does live our values and bring the market offerings that we always hoped to bring to Kiwis. As LHF have access to financial reserves, this will allow for product development, that will ultimately provide the consumer, both domestic and overseas, with new and interesting products. Thus, we see this as not only as beneficial to New Zealanders but also for export earnings. This acquisition seems, to us, to be a natural fit e.g., Chalmers Organics and LHF, as our respective company values are similar.

Further to that we also note that **all** brands (Bean Supreme, Lisa's, Naked etc) acquired by LHF over the last 20 years have grown in their offerings, strengthened their image and NOT increased or controlled pricing or competition. This is the reason that Chalmers sees this merger as the right one for our consumers. It has been very difficult for us to find any investor or company to work with, that we can trust and that that trust is proven historically in their actions. Chalmers would like to state that this acquisition is for the benefit of consumers because it will substantially increase product range. We are pleased to have found a partnership that we can trust and who lives similar values, and we are excited about growing our brand offerings with LHF, in the same way as is evidenced in regard to the aforementioned brands they now have.

## **SUPERMARKET SALES DETAIL YEAR March 2021**

Foodstuffs retail sales total	Countdown retail sales total	Foodstuffs South Island	<b>Total European Supermarket Revenue</b>	total vegetarian chilled sales (mat 28/03/21)	total vegetarian chilled sales percentage of supermarket sales	total tofu sales in European supermarkets (mat 28/03/21)	<b>total tofu sales percentage of supermarket sales</b>
\$7.5B	\$7.1B	\$3.2B	<b>\$17.8B</b>	\$39.6M	<b>0.2%</b>	\$9.5M	<b>0.06%</b>