

Foodstuffs North Island Limited and  
Foodstuffs South Island Limited  
Response to submissions on Commerce  
Commission statement of preliminary  
issues

**PUBLIC VERSION**

7 March 2024

Confidential material has been removed. Its location in the document is denoted by [ ].

## OVERVIEW

- 1 Foodstuffs North Island (**FSNI**) and Foodstuffs South Island (**FSSI**, together, the **Parties**) welcome the submissions<sup>1</sup> and other feedback on the Commerce Commission's (**Commission**) statement of preliminary issues, and the opportunity to provide responses to points raised in them. These responses are not intended to represent a comprehensive articulation of the Parties' views on the competition law merits of the Proposed Transaction. The Parties' responses are set out at **Appendix A** and an independent expert economist report from Houston Kemp is at **Appendix B**.
- 2 The Parties note that submissions and other feedback raise a number of issues that are not related to the Proposed Transaction, or to its potential effect on competition. While they fall outside the scope of the Commission's merger clearance analysis, the Parties welcome the tabling of these issues, and look forward to engaging with the Commerce Commission and other stakeholders on improving our industry.
- 3 In addition, the Parties note the statements made in submissions suggesting there is a different rationale for the merger than the Parties have indicated. The rationale of the merger is to create a world-class, customer-driven national food and grocery retailer and wholesaler. More specifically, the rationale of amalgamating the management and operation functions of the two co-operatives' support centres, is to achieve cost reductions (including overhead costs and product costs), efficiency gains, increased agility and innovation and a more cohesive national offering, which would ultimately deliver better value for customers at the checkout. The claims that this is not the true rationale derive from a lack of understanding of the co-operatives and their structure. In any event, the Commission has access to relevant internal documents and other materials to test that the Parties have accurately described the rationale.

---

<sup>1</sup> The submissions are:

- Anonymous A submission on the Application dated 22 January 2024,
- Anonymous B submission on the Application dated 23 January 2024,
- Anonymous C submission on the Application dated 25 January 2024,
- Habilis New Zealand submission on the Application dated 31 January 2024,
- Ernie Newman revised submission on the Application dated 5 February 2024,
- Grocery Action Group submission on the Application dated 9 February 2024,
- The Warehouse Group submission on the Application dated 9 February 2024,
- Lisa Asher submission on the Application dated 9 February 2024,
- Food and Grocery Council submission on the statement of preliminary issues dated 19 February 2024,
- Northelia NZ Submission on Merger of Foodstuffs North and South Island, 27 February 2024, and
- Monopoly Watch Foodstuffs merger clearance submission evidence, 27 February 2024.

## APPENDIX A – RESPONSES TO THE SUBMISSIONS

### Anonymous A

#### ***The merger will result in reduced product innovation (i.e. reduced choice for consumers and ability for suppliers to test product viability).***

- 1 This concern appears to arise from an expected increase in buyer power associated with the Proposed Transaction. In the Parties' view, the Proposed Transaction will not result in reduced product innovation arising from effects on competition for the acquisition of groceries. The additional point about suppliers' ability to test product viability is considered below from 8.
- 2 The Commission's framework for considering buyer power provides that a merger between competing buyers may lessen competition if it increases the merged firm's ability to exercise market power when buying products. Buyer market power is described as "the ability to profitably depress prices paid to suppliers to a level below the competitive price for a significant period of time such that the amount of input sold is reduced".<sup>2</sup>
- 3 The Commission makes its assessment by comparing buyer power in the factual and counterfactual, and determining whether competition would be substantially lessened comparing the two scenarios.
- 4 The Houston Kemp report at **Appendix B** sets out the appropriate framework for considering this question. Consistent with the Commission's previous work, and the ACCC's 2008 grocery market inquiry, Houston Kemp explains that interactions between grocery suppliers and the Parties is most appropriately assessed by reference to a "bargaining framework".<sup>3</sup> That is because supply arrangements tend to be established by bilateral bargaining between the supplier and grocery retailer. When considering the effects of a merger where the bargaining framework is appropriate, the commercial realities of the interactions between *particular* suppliers and buyers are important. That is, what are those suppliers' options, and how would they be affected by the Proposed Transaction?
- 5 As such, the key question for consideration is whether, for any given supplier (or type of supplier, or product) the Proposed Transaction would result in a change in the dynamic such that competition would be lessened e.g. the merged entity would have an incentive to withhold demand and/or depress prices so much and for such a period that competition is lessened. A buyer's ability to achieve lower prices is not in and of itself a lessening of competition – it is either neutral (a transfer) or, to the extent it results in cheaper products to consumers, pro-competitive. For lower supply prices to be detrimental to competition, more is required.
- 6 First, and importantly for the analysis of all relevant supply relationships, there will be no change to the merged entity's incentives to compete downstream, compared with the status quo counterfactual. That is because the Proposed Transaction will not give rise to any change in concentration in any retail grocery market. As such, there will be no difference between the factual and counterfactual in terms of incentives to compete downstream (including as regards procuring products to supply at retail).

---

<sup>2</sup> Commerce Commission, *Mergers and Acquisitions Guidelines*, May 2022 at 4.2.

<sup>3</sup> See part 2.2.

7 Secondly, the spectrum of options for suppliers will not be affected by the Proposed Transaction such that there could be the potential for an adverse impact on competition. Houston Kemp applies the relevant bargaining framework to describe the expected impact on the acquisition of fresh products, which the Parties understand to be an area of potential concern – see Part 4 of the report. The Parties have provided the following examples to further illustrate the position for fresh products. The Parties have focused on products where there is not high supplier concentration and therefore significant market power on the supplier side (e.g. milk), where concerns are even less likely to arise:

7.1 *lemons* - in the year ending 30 June 2023, approximately 37% of domestic production was exported,<sup>4</sup> with New Zealand also importing lemons as well as producing them domestically. While the Parties are unable to provide figures, they understand that domestic foodservice customers are also important buyers, alongside grocery retailers (the Parties understand lemons are particularly important to such customers). In the Parties' experience, export and import prices are the key influence over the price of lemons. For example, suppliers have the option of increasing exports, and FSNI notes that the establishment of new imports can help to push domestic supply prices down. As such, suppliers' outside option of exporting is likely to be a key factor in their willingness to accept terms from any particular domestic buyer. The merger of two domestic purchasers would not make a material difference.

Other fruit and vegetables, such as cherries and apples, as well as a high proportion of meat and seafood, have similar dynamics, where export is a key outside option and drives bargaining outcomes,

7.2 *potatoes* – for some fresh products, exports are not so readily possible. Because of potatoes' use in ingredients such as chips, suppliers' alternatives include large multi-national processors such as Kraft Heinz, PepsiCo (to produce Bluebird products), Griffins Foods (to produce Eta products) and McDonalds. These options (as well as any exports) are a key driver of prices for potatoes and would not change as a result of the Proposed Transaction.

Fresh products that can be canned, and those that are used as ingredients (including many fruits such as plums and apricots, plus vegetables such as corn and tomatoes), are subject to similar dynamics, where supply to major (in many cases, global) buyers for alternative uses influence bargaining outcomes. The change arising from the Proposed Transaction cannot materially alter this position, and

7.3 *green vegetables* – for highly perishable fresh products, only local supply is feasible, and transporting these products over the Cook Strait is a material hindrance in terms of time and cost. For such products, supply generally takes place to single stores or, at most, an island, and comes from suppliers in the same island. For such products, the Proposed Transaction is not capable of affecting bargaining outcomes as it would not give rise to any change in bargaining dynamics – it is already the case that generally only one co-operative (or one or more of its stores) is acquiring from relevant suppliers, and that will not change as a result of the Proposed Transaction.

---

<sup>4</sup> United Fresh New Zealand Incorporated, *Fresh Facts 2023: New Zealand's Fresh Fruit and Vegetable Industry*, 14.

**The current structure enables suppliers:**

- **to test a product in a smaller operation to prove its viability. If one co-op doesn't take the product, suppliers can go to the other co-op, and**
- **to have two opportunities at ranging their products, with the co-ops undertaking ranging reviews at different times in the year.**

**FSNI's centralised range reviews are evidence of this problem (with suppliers only having one opportunity to try to get products stocked).**

- 8 The Proposed Transaction will not change the ability for a product to be tested in a smaller operation to prove its viability. There will be no fewer opportunities to engage locally (and in the Parties' view it should ultimately be easier to engage with the merged entity than with the existing co-operatives).
- 9 Supply to a single store, and a small number of stores, is an important feature of both FSNI and FSSI's business currently (even where the centralised buying practices are in place – see further below from 22). For both co-operatives, it is a highly valued way in which to foster new suppliers and the supply of new products, by allowing suppliers to test the viability of new products, and expand their capability and capacity to supply over time.
- 10 Local buying allows the Parties to find and foster new and innovative local products that:
- 10.1 have a particular constituency in a local area and therefore improve their local competitive positioning, and/or
- 10.2 with some fostering and development, could provide a new and attractive island- or nation-wide product offering.
- 11 Both co-operatives' centralised buying has a "local range" category, which includes products that are ranged in a single store or a smaller number of stores. To further encourage such local supply, each co-operative runs a programme to find and facilitate smaller suppliers' development. FSNI has also launched the Emerging Suppliers Forum – see below from 12 for further information).
- 12 For example, [ ]]. [ ]].
- Further, the Emerge competition (where new and small suppliers compete to be ranged in Foodstuffs supermarkets) and Emerging Supplier Forum (through which FSNI seeks to engage with emerging suppliers across the country in order to bring new products to market) are evidence of these incentives. As part of the Emerging Supplier Forum, FSNI ran 16 forums in the last 12 months with approximately 260 attendees, [ ] follow up contacts and [ ] new suppliers being ranged or actively worked on being ranged. This forum is expected to continue following the Proposed Transaction.
- 13 There is no plan, and no incentive, for this feature to alter as a result of the Proposed Transaction. That is, both co-operatives regard local supply as an important competitive advantage over their (corporate) competitors, which is facilitated by the presence in local communities of store owner-operators (who themselves have an interest in supporting local suppliers for their own competitive

advantage).<sup>5</sup> Corporate competitors do not have a local ownership presence and, in the Parties' view, are much less well placed to identify and "get in on the ground floor" of the best new products.

- 14 The co-operatives have no incentive to cease a practice they perceive as a key competitive advantage, and a key method of ensuring they remain at the forefront of product innovation. Post-merger, the same value will be placed on the ability to foster new suppliers and products by starting in a smaller operation, and there will be the same number of local stores, with the same number of local owners, and therefore the same ability to provide this offering to new suppliers.
- 15 These conclusions are supported by the framework set out in the Houston Kemp report as to the position of smaller suppliers (see section 3.3 of the report).

***The merged entity will be considerably more powerful, with increased ability to resist a new competitor entering and establishing itself in the market.***

- 16 No reasons are given, so it is not clear the basis for this concern. However, given the focus of this submission is the acquisition of groceries, the parties note that the merger is not expected to increase buyer power such that a substantial lessening of competition could result. See further above at 1. There will be no change in terms of the Parties' presence, scale or volumes acquired.

**Anonymous B**

***The merger will not reduce grocery costs to consumers through the strengthening of buying power.***

- ***Vast majority of suppliers supply at their best prices, with the same pricing to Woolworths and Foodstuffs.***
  - ***Both Woolworths and Foodstuffs enforce a 35% margin on groceries plus additional rebates.***
- 17 This submitter raises a concern that the merged entity will not be able to achieve better buying prices, given the co-operative already achieves the best viable prices in the market. The Parties acknowledge there is real uncertainty as to the extent of the better pricing that will be achieved, which is supported by the economic evidence at **Appendix B.** [

].

- 18 The parties do not know the source of the submitter's statement that the "vast majority of suppliers supply at their best prices, with the same pricing to Woolworths and Foodstuffs" and have no visibility over the prices Woolworths currently achieves. However, they acknowledge that any product price savings that may arise from the Proposed Transaction are subject to the outcome of negotiations with suppliers – see also **Appendix B.** [

].

---

<sup>5</sup> For example, [

].

- 19 It is not correct that FSSI and FSNI “enforce a 35% margin on groceries plus additional rebates”. FSNI and FSSI do not have any knowledge of Woolworths’ margins. The Parties note the Commission obtained margin information during the market study.
- 20 It is also worth noting that the concern raised in this submission, if correct, would suggest the Proposed Transaction could not give rise to any lessening of competition associated with the acquisition of groceries because the Proposed Transaction would not alter bargaining outcomes.

***The merger will reduce product innovation.***

- 21 No reasons are given, so it is not clear the basis for this concern. However, given the focus of this submission is the acquisition of groceries, the parties note that the merger is not expected to increase buyer power such that a substantial lessening of competition could result. See further above at 1.

***Many suppliers only provide products to one of the co-ops. The merger will result in centralised buying which will be based on product performance. Small/medium sized suppliers will be put out of business (especially in the South Island) as they are unlikely to be selected for national ranging.***

- 22 Both co-operatives engage in, and are developing, centralised buying practices (with FSNI more advanced in its adoption). Centralised buying would continue with or without the merger for both co-operatives. In other words, the advent of the Proposed Transaction does not affect whether centralised buying will be a feature of FSSI’s procurement practices.
- 23 Regardless, the Houston Kemp report at **Appendix B** demonstrates the Parties’ view that the relative bargaining position of the Parties in the factual and counterfactual will not be materially different with respect to smaller and larger suppliers. In any event, it is worth noting there is already a more than [ ] overlap in stockkeeping units as between the Parties so their ranges are already closely aligned.
- 24 It is important to note that centralised buying does not eliminate the ability of suppliers to supply a single island, or a single store. The Commission has previously described centralised buying as being where “product ranging decisions are made centrally at the retailers’ head office”.<sup>6</sup> It is the *decision* that is made centrally; it is not the case that the range of *outcomes* needs to be limited to island-wide supply (see from 8 above for further discussion). For both co-operatives, local stores retain the ability to carry out local ranging.<sup>7</sup>
- 25 It can be assumed that rational decision-making applies to each co-operative’s choices, and that that would continue following the Proposed Transaction. It would not be rational for the merged entity not to range a supplier’s products in only one island, region or other grouping where doing so allows the merged entity to be more competitive. This may occur in a range of scenarios, for example, where:

---

<sup>6</sup> Market study final report, 8.15.

<sup>7</sup> [

].

- 25.1 for highly substitutable products, the supplier's cost structure allows that supplier to be price competitive supplying a single island (but not both islands),
- 25.2 a supplier has a product that is particularly preferred by consumers in one island, region, or at stores in areas with particular demographic characteristics, or
- 25.3 a supplier whose products would be popular nationally but which has the capacity to supply only one island.
- 26 Even if the personnel making these decisions change following the merger, that is not a merger effect of the type the Commission considers (personnel changes can occur at any time and are not attributable to a merger as such).

*Store owners foster smaller suppliers and that would continue following the Proposed Transaction*

- 27 In terms of the merger effect for suppliers that supply a single store or a small group of stores: no change to local store ownership will arise from the Proposed Transaction, so there is no reason to expect local decision-making to change. The current practice is presumably rational, and there is no structural change arising from the merger that would alter that.
- 28 In fact, the Parties consider their ability to identify, and foster the development and growth of new suppliers through individual local stores is a key advantage they hold over corporate competitors, which they observe not to have such flexibility (see above from 8). As such the Parties are strongly incentivised to continue with this practice. The extent of local ranging is illustrated above at 12.

### **Anonymous C**

***The current structure offers suppliers a chance to negotiate and reach different consumer bases through the distinct South Island and North Island operations. This would be lost through the merger. The merger risks further disadvantaging suppliers (e.g. less bargaining power, less favourable terms and squeezing margins).***

***FSNI's centralised buying is problematic.***

***FSSI's decentralised approach enables suppliers to contact local stores directly to get their products ranged which is especially important for new suppliers.***

- 29 As noted from 22 above:
- 29.1 FSSI is progressing its rollout of a more centralised buying model, which it would continue to do in any counterfactual. As such, the advent of centralised buying is not a merger effect for FSSI, and
- 29.2 centralised buying does not eliminate smaller suppliers' ability to obtain local ranging, or to contact individual stores and be ranged in a single, or small number, of stores.
- 30 Further, it is not uncommon for both co-operatives to absorb part or all of a purchase price increase from a supplier (i.e. they do not pass on the full amount of the increased cost to the consumer, resulting in them receiving a lower margin). Currently, both co-operatives are focused on absorbing purchase price increases from suppliers on key household items, in light of the high-inflation environment. Recent examples of where FSNI has not passed on all, or any acquisition price increases to customers, include [



]. [

]<sup>8</sup>

30.1 [

],

30.2 [

], and

30.3 [

].

***The merged entity will be able to use its increased market power to influence pricing and service quality. There will be an increased risk of coordinated behaviour which could lead to higher prices and reduced output.***

- 31 The Parties are not able to detect precisely the concern being raised when the submitter says “the merged entity will be able to use its increased market power to influence pricing and service quality”. However, it appears to be linked to the concerns about the position of smaller suppliers, as to which see above at 8 and 22.
- 32 The Parties also do not consider the Proposed Transaction will increase the prospects of coordination in relation to the acquisition of groceries. In considering coordinated effects in the merger context, the Commission assesses whether:
- 32.1 a market is vulnerable to coordination, and
- 32.2 a merger changes the conditions in the relevant market so that coordination is more likely, more complete or more sustainable.
- 33 The Proposed Transaction will not change the conditions in the relevant market to increase the likelihood of coordination.<sup>9</sup> The Commission identifies a number of market features in its Mergers and Acquisition guidelines that it considers may facilitate coordinated conduct. These are set out below, along with comments on the likely effects of the Proposed Transaction on these market features:
- 33.1 *homogenous products*: the Commission acknowledged in the market study that the high degree of product and brand differentiation and large number of products sold by the major grocery retailers are features of the market that hinder accommodating behaviour. The number and range of products and brands acquired and sold by the merged entity would not change as a result of the merger. Therefore, this market feature will be unchanged,

---

<sup>8</sup> [

].

<sup>9</sup> As mentioned in the clearance application, the Parties do not agree with the views expressed by the Commission in the 2022 market study, that retail grocery supply has some features that make it vulnerable to coordination and that there is evidence that suggests the potential for coordination in relation to the acquisition of groceries.

- 33.2 *a small number of competitors and an absence of a particularly vigorous competitor or strong competition from outside the coordinating firms:* the Parties do not compete in downstream markets (with each co-operative focusing on competing in the island in which it is based). The Proposed Transaction would not reduce the number of competitors. The result is that there would be no change to the market in this regard,
- 33.3 *firms repeatedly interacting through, for example, numerous, repeated transactions, through contact in other markets or other repeated interactions, for example, through industry organisations or meetings (e.g. to set technical standards):* the major grocery retailers do not interact directly (e.g. through transactions, or beyond small interactions in industry forums) or indirectly (e.g. through suppliers, given suppliers do not offer information regarding Woolworths to FSNI and FSSI and, the Parties assume, vice versa). This will not change as a result of the Proposed Transaction.

As mentioned in the clearance application, irrespective of whether and to what extent suppliers seek to avoid promotional clashes between the major grocery retailers, suppliers will not have increased visibility of competitive strategies as a result of the merger,

- 33.4 *firms of similar size and cost structures:* in the context of the acquisition of groceries, we understand suppliers' concern is that Woolworths and the merged entity would be better positioned to deduce each other's offer to and arrangements with suppliers such that they could coordinate and/or accommodate each other's offers and arrangements (see the point made in the New Zealand Food and Grocery Council's submission below at 111). This is not a realistic consequence of the Proposed Transaction given the breadth of products supplied by each of Woolworths and Foodstuffs, the components other than the product cost that make up product acquisition costs (e.g. trade spend) and the different retail pricing and promotional activities that apply to products (such that it would not be possible to "work backwards" from the retail price to determine product acquisition costs).

Further, the Parties do not consider the merged entity would have the same cost structures or necessarily be a similar size to Woolworths New Zealand. In fact, Woolworths Group (Australia + NZ) is much larger than the merged entity. In addition, Foodstuffs operates different banners while Woolworths' operations are mostly under the Countdown/Woolworths brand. All banners have different positioning which means the strategies are very different (value vs customer experience). Foodstuffs assumes that, as a corporate with a single strong banner, Woolworths would have a simpler cost structure and would also follow the Australian model in many aspects, such as pricing/promotions strategy, marketing, property, private brands, loyalty, ecommerce and digital. FSNI and FSSI also observe many differences in their operations, which could affect cost and cost structure. These features all create complexity and render the businesses not easily comparable,

- 33.5 *little innovation, stable demand and lack of supply shocks/volatility:* as described in the clearance application, the Proposed Transaction would not result in material or adverse changes to the volumes of grocery products acquired from suppliers by the Parties (unless cost efficiencies led to lower prices which in turn, increased customer demand at the merged entity's stores), such that any existing features of the market regarding supply and demand stability/volatility will be unchanged. Further, no reduction to the level of innovation of the Parties is expected. Rather, the Parties anticipate

an increased ability to innovate as a result of the merged entity being a more efficient and agile operation compared to the two separate co-operatives,

33.6 *firms that can readily observe each other's prices or volumes*: the points described above at 33.4 in relation to firms of similar sizes and with similar cost structures, equally apply in relation to this market feature, and

33.7 *firms interrelated through association or cross-partial ownership*: this feature is not relevant as no such interrelation between Foodstuffs and Woolworths exists or will exist following the Proposed Transaction.

***Supermarket home brands undermine the viability of smaller and local suppliers due to the aggressive promotion and pricing of these products. This hampers other suppliers' ability to innovate and invest in their products.***

34 The position of private label will be unaffected by the Proposed Transaction, since private label activities are already conducted by the Parties jointly. It can be assumed that the private label strategy is already optimised nationally on the basis each Party is operating rationally in meeting the needs of consumers in retail markets they serve, and there will be no change in any local market arising from the Proposed Transaction.

35 In any event, the Parties disagree with this characterisation of private label. The Parties' private label business is run separately to the co-operatives, through Foodstuffs Own Brands Limited (**FOBL**). Private label products are evaluated by the Parties against the same criteria as branded products, measured against the same performance guidelines and go through the same category review processes. These products do not get a "free ride". As part of these processes, the Parties have a history of choosing to remove private label goods from product categories and amending the ranging of private label products to be less favourable, in the same way they would branded products (and this is covered by the Code – see 40.3).

36 [

]. [

].

37 The Parties' private label offering was first developed in response to suppliers of commoditised products having a strong negotiating position. The purpose of private label products was and is to improve competition and consumer choice, not reduce it.<sup>10</sup>

38 In any event, it is far from clear that an increase in the supply of private label products would have an adverse effect on competition. The Commission recognised in the market study that there could be benefits to private label (lower costs, more consumer choice) but that they could also be harmful to consumers (e.g. by ultimately reducing consumer choice), particularly where the market was concentrated. Currently, the penetration of private label is not particularly

---

<sup>10</sup> See the Parties' comments in the market study final report at 3.179.

significant, its share has [ ] over the last 5 years, and private label products face strong competition.

***The Commission should consider alternative approaches to the proposed merger such as:***

- ***Conditional merger approval on splitting the banners (e.g. PAK'nSAVE and New World/Four Square).***
- ***Require the distribution centres to be independent, neutral logistics depots so these could fairly service a variety of retailers.***
- ***Eliminate supermarket home brands.***
- ***Prohibit loss leader strategies (on the basis that this tends to require increased prices for other products to set off the loss).***

39 An applicant for clearance may offer divestments where that would remedy an identified competition concern. The Parties' position is that no lessening of competition can arise from the Proposed Transaction and therefore no divestment remedy need be offered. The Parties further note that some of the suggested remedies fall outside the scope of the clearance process.

40 It is, however, worth noting that many of these suggestions are being implemented in some form. For example:

40.1 the wholesale access regime under the Grocery Industry Competition Act 2023 (**GICA**) effectively requires the Parties' distribution centres to service other retailers,<sup>11</sup>

40.2 there is a focus on pricing through both the Commission's enforcement activities under the Fair Trading Act 1986 and the new unit pricing regulations,<sup>12</sup> and

40.3 the new Grocery Supply Code provides specific protections of suppliers' intellectual property in light of retailers' interests in private label products and requires non-discrimination of private label products in range reviews, product ranging decisions and shelf space allocation decisions.<sup>13</sup>

**Ernie Newman**

***The Commission should investigate the co-ops current non competition. Even if the current arrangements are not illegal the two co-ops could compete in a number of different ways which would enhance the countervailing power of suppliers.***

41 This submission and others suggest the Parties' existing business model may be flawed with respect to the requirements of the Commerce Act 1986. There is a further suggestion that the Commission's counterfactual analysis should include an assumption that the flaws are rectified. With those flaws rectified, the suggestion is that there is a real chance the Parties would be in competition with each other. The upshot would be the Commission would need to compare the effects of the Proposed Transaction against a counterfactual in which the Parties compete with each other.

---

<sup>11</sup> See Part 3 of the GICA.

<sup>12</sup> See the Commission's case register regarding its Fair Trading investigations into FSNI, FSSI and Woolworths' pricing and promotional practices and the Consumer Information Standards (Unit Pricing for Grocery Products) Regulations 2023.

<sup>13</sup> Clauses 24, 26 and 27 of the Grocery Supply Code 2023.

- 42 The Parties do not consider their current business model to entail any breach of the Commerce Act, for the reasons given below.

*The Parties' current business model is lawful*

- 43 The Parties each focus on maximising the competitiveness of the retail banners in the island where they operate. That there are separate co-operatives is a result of the historical development of the Foodstuffs business. Historically, a number of co-operatives operated, each with a focus on the geographic area it was located in. As time went on, the logic of having separate "hubs" reduced, with the increased costs of systems, and the ability to reduce the duplication between the "hubs". As suppliers also increasingly became larger, and national and multinational operations, operating through bigger "hubs" made more sense. As such, over time the co-operatives have merged.

- 44 Under the existing business model, inevitably some assets (principally the brands) are shared between the Parties, with each using those assets in the island it focuses on. The Parties are undoubtedly in a collaborative activity as that term is used in the Commerce Act. However, there are no agreements that prevent the Parties from establishing a retail grocery business in the other island. As a matter of fact, there is not a real chance they would do so. The current business model is each Party's focus, and it allows each to be an effective competitor, particularly against their closest local and national competitor, Woolworths. Over time, each Party has continued to take the view that the current business model is its best use of capital and efforts, and there is no reason to expect that to change in any realistic counterfactual.

- 45 To illustrate the clarity of that choice for each co-operative: each has a successful grocery retailing business. To establish in the other island would require a new physical supermarket business (including distribution and other supply chain infrastructure, as a store in another island without access to supply chain would not be practical<sup>14</sup>), and brand [

], in competition with existing market participants.

Compared with developing the business within the existing footprint, and liaising with the other Party to ensure a competitive national offering, this is self-evidently a less attractive proposition.

- 46 The Parties further note that the Commission has considered their business a number of times, including during the extensive market study. It would be surprising if there were unlawful aspects of the business model that had gone unnoticed until now.
- 47 Any specific questions for one or both co-operatives in relation to the above may be confidential and commercially sensitive, but the Parties welcome discussion with the Commission on them.

*There is only one realistic counterfactual*

- 48 As a result of the position described above, there is only one realistic counterfactual against which the Commission should consider the competition effects of the Proposed Transaction. That is the status quo, including its current trajectory for each co-operative (e.g. FSSI would continue to progress its centralised buying

---

<sup>14</sup> Further, each store in a co-operative ownership model must operate profitably, otherwise non-profitable stores would be cross subsidised by profitable ones, which is contrary to the co-operative philosophy.

programme, noting FSNI is adopting a similar programme but is more progressed with rolling it out).

49 [

].

50 As such, the Parties consider the Proposed Transaction cannot result in any lessening of competition in relation to the retail supply of groceries.

***No merger should be allowed unless the co-ops separate their wholesale and retail functions and split up the banners.***

51 An applicant for clearance may offer divestments where that would remedy an identified competition concern. The Parties' position is that no lessening of competition can arise from the Proposed Transaction and therefore no divestment remedy need be offered.

***The current structure supports coordination between competitors, and this will worsen with the merger.***

52 Mr Newman sets out several limbs relevant to this broader concern:

52.1 *Foodstuffs co-operatives fail to compete with each other* - see above from 41,

52.2 *tacit collusion with Woolworths by avoiding aggressive competition for market share* – the submitter links this concern to a concern about confusing pricing but it is not clear how these two concepts are linked. In any event, FSNI and FSSI both compete vigorously to win market share from Woolworths. For example:

(a) subsequent to the 2013 merger of Foodstuffs' Upper and Lower North Island co-operatives, [

],

(b) [

],

(c) [

15

---

15 [

].

],

(d) [

], and

(e) [

].

52.3 *deliberately confusing pricing tactics* - this concern, if true, does not appear likely to support coordination, as it would make monitoring a competitor's pricing more difficult. The Parties consider they do not engage in confusing pricing but in any event, there is no reason to expect any particular change in pricing tactics will be incentivised by the Proposed Transaction. The Parties have no plans to adopt different pricing strategies as a result of the Proposed Transaction, and

52.4 *there is visibility of competitors' terms of supply* - the Parties disagree with this point as they do not know the terms their competitors receive from suppliers. Further, the evidence presented to support the concern relates to an issue that took place between The Warehouse and its supplier, Sanitarium. Neither Party had any involvement.

#### **Habilis NZ**

***The merger will have no effect on competition in the market because there is no competition in the market. Instead of the factual and counterfactual the Commission should be asking whether the restoration of the market will be enabled or hindered by the merger.***

53 This submission presents a law reform proposal. As such, it falls outside the scope of the existing process and may be more usefully directed at the Minister of Commerce or the Ministry for Business, Innovation and Employment.

#### **Grocery Action Group**

***The merger will decrease competition by further concentrating market power and reduce the range of products available to consumers, while strengthening barriers to entry.***

54 No evidence or theory of harm is presented as to this asserted merger effect. Related points are covered elsewhere in this submission.

***There is no evidence the merger will result in lower prices. Lower costs therefore lower prices at the till were promoted as a benefit for consumers of the 2002 Woolworths/Foodtown merger and again in 2013 with the merger of Foodstuffs' Upper and Lower North Island co-operatives.***

55 The Parties are not privy to whether and to what extent any benefits arising from the 2002 Woolworths/Foodtown merger were shared with consumers. In relation to the merger of Foodstuffs Upper and Lower North Island co-operatives, see below at 63.3.

***The merger will result in suppliers being shut out of the market, particularly in the South Island, as centralised buying will inhibit suppliers' getting their products directly into individual stores. This avenue is particularly important for smaller, new entrant suppliers.***

56 This part of the submission focuses on concerns that are also raised in Anonymous C's submission. As such, see above from 29.

***There may be cartel-like issues to be investigated in the merger proposal.***

57 This part of the submission focuses on concerns raised in Ernie Newman's submission, which are refuted above at paragraph 41.

***Alternative of splitting New World and PAK'nSAVE proposed. Hold off further consideration until the first industry annual report is published.***

58 As above, an applicant for clearance may offer divestments where that would remedy an identified competition concern. The Parties' position is that no substantial lessening of competition can arise from the Proposed Transaction and therefore no divestment remedy need be offered. The Parties further note that the second point falls outside the scope of the clearance process.

***The merger will make any future divestment more difficult (should current measures fail to create competition in the market).***

59 This concern is not an effect on competition of the Proposed Transaction, rather it is a comment on the potential practical impact of the Proposed Transaction on the Government's policy options. In any event, it is not clear how the Proposed Transaction would materially impact the Government's options in this sense, given no change to the physical distribution infrastructure is proposed (nor would be practical, given the Parties' respective retail footprints are geographically separate).

#### **The Warehouse Group**

***The stated rationale of the merger is to generate cost efficiencies which will be passed onto consumers. Similar statements were made in 2013 regarding the Upper North Island / Lower North Island merger and there is a real question whether any of the promised benefits from that merger ever eventuated.***

60 The rationale of the merger is to create a world-class, customer-driven national food and grocery retailer and wholesaler. More specifically, the rationale of amalgamating the management and operation functions of the two co-operatives' support centres, is to achieve cost reductions (including overhead costs and product costs), efficiency gains, increased agility and innovation and a more cohesive national offering, which would ultimately deliver better value for customers at the checkout.

61 Strictly speaking, it is not necessary for the Commission to conclude that cost savings would be passed on to consumers to the extent (as the Parties consider to be the case) the merger would not give rise to a substantial lessening of competition.



- 62 Nevertheless, the Parties consider there is good reason to conclude the merged entity would face significant competitive and regulatory pressure to pass on cost savings – see further below at 66.
- 63 Further, the Parties disagree with The Warehouse Group’s comments about the 2013 merger of the Upper and Lower North Island co-operatives, as follows:

63.1 **Submitter comment:** *FSNI stated that customers and members would benefit from all operations running under one IT system and integration of back-office functions. The integration of systems has been slow and it is unclear whether a truly integrated system now exists across FSNI (e.g. still referencing integration in the 2016 financial report, the roll out of the SAP system wasn’t in play for all of PAK’nSAVE, New World and Four Square until 2020).*

**Parties’ response:** This is not an accurate description of the systems integration that was achieved following the merger. FSNI had a fully integrated SAP enterprise resource planning solution in 2015, within two years of the merger announcement. This provided shared services across all of FSNI for merchandising, finance and procurement while supporting Foodstuffs Wellington stores and distribution centres in their existing technology stacks.

The statement that "SAP wasn't in play for all PAK'nSAVE, New World and Four Square until 2020" is also factually incorrect as the store rollout of the SAP store solution to PAK'nSAVE, New World and a chosen number of Four Square stores completed in 2018,

63.2 **Submitter comment:** *FSNI would be able to launch online grocery delivery that Countdown was already offering in 2013. This has been slow and incompletely delivered on (e.g. New World launched click and collect and online delivery in 2017 and as of the market study, PAK’nSAVE only had a click and collect option).*

**Parties’ response:** The pace and timing of the e-commerce rollout across FSNI occurred in accordance with strategic business planning from the time of the merger and was iterative in nature. Further, the development of FSNI’s e-commerce solutions accelerated FSSI’s rollout of e-commerce solutions to South Island stores. The PAK’nSAVE Click-and-Collect function is a complete solution based on a strategic, brand-aligned decision. Specifically, Click-and-Collect is the lowest cost option to supply online e-commerce orders to customers which is consistent with PAK’nSAVE being a value-based brand.

63.3 **Submitter comment:** *Systems integration would mean efficiencies and savings, translating into better services and lower prices over time. Distribution of profits to members have increased (e.g. 2015 and 2016 annual reports refer to increased profit distribution, as opposed to decreased prices)*

**Parties’ response:** This statement regarding efficiencies was made by Murray Jordan and published in a Stuff article released on the day of the 2013 merger.<sup>16</sup> In conjunction with this statement, Mr Jordan also commented:

---

<sup>16</sup> Laura Walters for Stuff, *Foodstuffs merger 'good for customers'*, 1 September 2013, <https://www.stuff.co.nz/business/9107913/Foodstuffs-merger-good-for-customers>.

PAK'nSAVE prices were currently 10 per cent below its nearest competitor, Countdown... Foodstuffs North Island would be able to drop those prices further as a result of the merger

Following the merger, which occurred in September 2013, [

].

For New World, there was an immediate change following and, in FSNI's view, attributable to the merger. [

].

- 63.4 **Submitter comment:** *The merger was about growth with every new PAK'nSAVE creating up to 200 jobs and New Worlds creating 100 new jobs. The merger did not appear to offer growth, or significant amounts of new jobs. FSNI has 395 more employees and 23 fewer stores. The first annual report after the merger noted a reduction in salary and direct employee costs (2015 Report).*

**Parties' response:** This is not an accurate representation of Mr Jordan's comments in the article. The article also states, "Jordan said some job cuts would be inevitable, especially as the company went through the process of cutting two executive teams down to one".

The figures presented are also incorrect. The number of PAK'nSAVE and New World stores has increased from 40 and 98 to 45 and 108 respectively between 2014 and 2023 (see FSNI's Annual Reports for these years). Only the number of Four Squares has declined over time. The total number of FSNI employees has also increased from approximately 22,000 to 24,000 between 2014 and 2023.

- 63.5 **Submitter comment:** *The merger was not expected to change profitability, the merged entity would sell more. However, between 2015 to 2023 profit has increased off a lower revenue base.*

**Parties' response:** It is worth noting that during the years compared, there was a change in accounting treatment adopted by FSNI that affected these figures such that some of the figures are not a like for like comparison. Specifically, in April 2018, FSNI adopted NZ IFRS 15 Revenue from Contracts with Customers. Although no significant changes in the timing of revenue recognition were identified as a result of the adoption of NZ IFRS 15, following a detailed analysis of the agency versus principal rules relevant to NZ IFRS 15, FSNI identified instances where revenue is now recognised net of the related expenses, and not gross as it would previously have been reported. This results in a decrease in both revenue and expenses, with no impact on net profit. This change in revenue recognition meant that from FY19 onwards, revenue reported in FSNI's statutory accounts is under the different

treatment. [ ]].

The profit reflected in FSNI's financial statements is affected by a number of factors related to the co-operative's operating model between its member shareholders, including monthly direct charges to its members, and in year annual expenditure and recovery of historic annual expenditure from members via levies. Because of this, the net profit reported in 2023 is not on a like for like basis with 2015.

***How can the Commission be confident the efficiencies provided by the merger will not give the merged entity a profit buffer to be able to withdraw from low margin areas and focus on growing its footprint in other more profitable areas to saturate the market with Foodstuffs branded stores? Are store closures or new stores modelled? If so, could the merger result in small markets left without a supermarket?***

- 64 No change in retail strategy is proposed or would be incentivised as a result of the Proposed Transaction. If it were rational to withdraw following the Proposed Transaction, then it would be rational to withdraw currently and in the counterfactual.
- 65 The logic of the submitter's point is unclear. That is, if the merged entity required a profit buffer to withdraw from low-margin areas, that would suggest withdrawing from such areas would reduce its profits, therefore withdrawing would not be rational. Both co-operatives consider their current retail strategy is rational within the areas they operate. The Proposed Transaction is not expected to alter that feature (it is not clear how it could) and accordingly this concern appears unfounded.

***The clearance application states that the Commission can rely on the GICA to fix any issues and make sure savings are passed through to consumers. This assumes the Commission has the power to deliver outcomes through regulation that are better than competition. Regulatory intervention also comes with a higher public cost. If there is a real chance that, as the bargaining power of the combined entity is enhanced, the public cost of more expansive regulatory intervention will be higher in the factual, then the Commission cannot be satisfied that the merger would not substantially lessen competition.***

- 66 This concern incorrectly records the points the Parties have made in the clearance application. The Parties do not consider the Commission can (or would need to) rely on the GICA to fix any issues and make sure savings are passed through to consumers. In fact, the primary pressure for the merged entity to conduct itself competitively arises from the market, with the GICA, and the Commission's role pursuant to it, safeguarding and extending this effect.
- 67 Specifically, the Parties consider retail markets are becoming more competitive, as a result of market developments such as the entry of Costco and Circle K, and the development of The Warehouse Group's grocery offering.
- 68 The measures taken pursuant to the GICA, and the public and policy pressure on the Parties, also promote further development of competition in the market, in particular by providing for wholesale access for market participants on a prescribed basis. These measures assist generally in facilitating retail competition (as well as providing monitoring and enforcement powers to the Commission). But they also assist specifically with regard to placing pressure on the merged entity to pass through any cost savings achieved in purchasing grocery products from suppliers,

onto regulated wholesale customers. This is because the GICA effectively requires a regulated grocery retailer to pass through discounts, payments or rebates received from suppliers as a result of the regulated grocery retailer's scale and efficiency of operations, to its regulated wholesale customers (i.e. retailer-customers).<sup>17</sup> If the merged entity, as it must, passes through such savings, then its retailer-customers will have the benefit of those savings when setting their retail prices. This, in turn, will place additional competitive pressure on the merged entity to share cost savings with consumers through its own retail prices.

***In response to the argument that the co-ops do not compete and that the merger will not result in increased bargaining power or a change in share of supply at both retail and wholesale, The Warehouse Group:***

- ***recommends the Commission carefully tests the suggestion that there is no merger specific change in volumes of wholesale purchases modelled by the parties in the factual. For example, the Commission could test whether the merger is intended to facilitate growth (which would presumably lead to increased volumes); and***
- ***considers that if no growth is modelled, but the merger is predicted to generate procurement synergies, then there is a real risk those synergies will include cost synergies arising from a reduction in the price of groceries acquired for wholesale supply derived from greater bargaining power of the merged entity.***

- 69 It is correct to say that, *to the extent any cost savings result in Foodstuffs stores having lower retail prices* than they otherwise would, and that in turn results in the merged entity's market share increasing, then it would give rise to incremental increases in the volume of products purchased. Of course, this would be a pro-competitive effect rather than an anti-competitive effect.
- 70 That said, there is no guarantee that lower retail prices will give rise to increased market share for the merged entity. Lower retail prices could well drive a competitive response from Woolworths, The Warehouse Group, Costco and other retailers (including those supplied under the GICA, which as above will benefit from product cost savings achieved by the merged entity). That response could mean the merged entity may not benefit, or benefit as much, from increased market share. Such a scenario would represent an increase in competition compared with the status quo (and counterfactual).
- 71 As to the impact on bargaining power, see above at paragraph 1, and **Appendix B**.

---

<sup>17</sup> Section 24 of the GICA sets out "other principles" that the Commission and Minister must take into account when deciding whether to perform or exercise their functions, powers or duties under the Act, and in performing or exercising them, to the extent that the Commission or Minister considers them relevant to the main principle in the Act. Relevantly, s24(1)(b) refers to "the desirability that wholesale customers have reasonable access to any discounts, payments or rebates made available to a regulated grocery retailer directly or indirectly by, or on behalf of, a supplier in connection with either or both of the following: (i) the scale of operations of the regulated grocery retailer and its associated persons, and (ii) the efficiency of operations of the regulated grocery retailer and its associated persons".

Section 46 of the GICA prevents a regulated grocery retailer from engaging in conduct that has the purpose or likely effect of preventing or restricting a wholesale customer from receiving the benefits of a range-, quantity-, or frequency-based discount, which includes such payments made available in connection with the scale and efficiency of operations of the regulated grocery retailer.

***Even where the co-operatives currently deal separately with the same supplier for nationwide supply, the Application suggests that the only change would be that one contract would be in place, rather than two and the merged entity's overall bargaining power will not be greater because they don't currently compete in relation to the share of supply. The Warehouse Group asks – Do FSNI and FSSI currently negotiate together on every wholesale supply arrangement? What agreements do they have about negotiating together? What practices do they engage in that leads to a lack of competition between them?***

- 72 See above at 1 and **Appendix B** regarding buyer market power, and at 41 regarding existing arrangements between the Parties.

***Even if there is no competition between the two co-ops there may still be a substantial lessening of competition caused by the merger through conglomerate or coordinated effects.***

***The conglomerate effects of the merger mean suppliers bargaining power would be materially reduced when dealing with a request for a single national supply contact (compared to dealing with 2 separate entities).***

- 73 Conglomerate effects arise where there is a merger of firms that supply products that may relate to each other (e.g. complementary products).<sup>18</sup> Conglomerate effects tend to include an increased ability or incentive to foreclose competitors or potential competitors through the tying and bundling of goods and services.<sup>19</sup> This should be distinguished from coordinated effects in relation to the acquisition of groceries which are addressed above from 32 .

- 74 The Commission in its statement of preliminary issues comments on potential coordinated effects of the Proposed Transaction but not on conglomerate effects. As discussed below at 77, it is not clear to the Parties how tying and bundling of grocery products, which is not currently a meaningful feature of grocery retailing markets, would be likely to become an issue following the Proposed Transaction.

- 75 Further, this part of the submission, rather than focusing on conglomerate effects, appears to reiterate the concerns it raises with respect to the position of suppliers. As to this issue, see above at 1.

***The Commission should consider whether the impact of the greater symmetry of scale and cost structures between the merged entity and Woolworths could increase the risk of coordinated effects, particularly in procurement of groceries for wholesale and retail supply.***

- 76 The Parties' views on coordinated effects in relation to the acquisition of groceries are set out above from 32.

---

<sup>18</sup> Commerce Commission, *Mergers and Acquisition Guidelines*, May 2022 at [5.11].

<sup>19</sup> At [5.12] to [5.15].

***There is currently a lack of effective competition in the market and the merger will worsen this, creating greater barriers to retail entry and expansion at scale.***

***The Commission cannot exclude a real chance that conduct described in the market study will remain a barrier to entry and expansion. This conduct is more likely to be made worse by the proposed strategic merger, based on an orthodox application of the conglomerate effects tests.***

***There is an incentive and ability to foreclose competitors with tying or bundling strategies (and other strategic conduct), including under the GICA.***

***Wholesale supply competitors are unlikely to facilitate a retailer stocking a limited range of SKUs, as The Warehouse Group found when Sanitarium refused to supply it with Weet Bix. Procurement of key staples from its retail competitors' wholesale arms is unlikely to deliver pricing that allows material undercutting of those competitors' own retail pricing.***

77 It is not clear how tying and bundling of grocery products would be likely to become an issue following the Proposed Transaction. Such practices are not a feature of retail or acquisition markets that is meaningful to competition at present, and it is not clear what changes would arise from the Proposed Transaction that would increase their likelihood. In particular, it is not clear what would motivate the merged entity, above and beyond the existing two co-operatives structure, to seek to increase the sale of products that are conditional upon consumers' purchase of other products.

78 The Parties are unable to comment on suppliers' willingness to engage in wholesale supply of a limited range of SKUs, except to say that they do not discuss this issue with suppliers and cannot foresee a scenario where the Proposed Transaction would change that. Suppliers are key competitors of the Parties in the wholesale supply of grocery products under the GICA regime, so such discussions would be inappropriate or, at worst, unlawful.

79 The Parties disagree with The Warehouse Group's statement that procurement of key staples from its retail competitors' wholesale arms is unlikely to deliver pricing that allows material undercutting of those competitors' own retail pricing. Regulated grocery retailers are compelled to pass through their scale benefits in pricing to regulated wholesale customers (see above at 68). Regulated wholesale customers' ability to undercut the regulated grocery retailers' pricing therefore depends only on the customers' costs and their ability to develop an attractive retail brand such that suppliers are willing for their products to be displayed and promoted through the channel. Any excess profits being earned by the regulated grocery retailers would provide additional headroom for other retailers to make a positive return (of course if, as the Parties consider to be the case, profits are not excessive, then this point diminishes in significance). None of the above would change as a result of the Proposed Transaction.

***FSNI appears to be quicker to innovate than FSSI. The Commission needs to be confident that the merger will not reduce the quality or pace of innovation from FSNI.***

80 It is not clear what evidence this concern is based on, as FSNI and FSSI do not perceive there to be a material difference between them in terms of the quality or pace of innovation. It is true that some internal innovations have begun within FSNI and FSSI has rolled them out subsequently e.g. centralised buying processes. That said, a number of innovations have originated within FSSI e.g. SHOP'nGO (which allows customers to scan and pack their items, as well as track their spend, as they shop), self-checkouts, the use of mobile handheld devices for retail operations management and New World Clubcard personalised promotions.

- 81 Innovation is focused on competing with other market participants, rather than each other, so it is not expected that the Proposed Transaction would generate any material difference in the quality or pace of innovation.

**Regulatory compliance: Gives the market study example that FSNI's Four Square stores could not offer unit pricing, as they do not have appropriate software. The Warehouse Group asks whether the merged entity will be prepared and equipped to comply with the existing, and future, regulatory regime? Will non-compliance of the merged entity impact the public through the cost of an increased need for input from the regulator?**

- 82 Each Party is working hard on compliance with the GICA, and both are committed to ensuring integration does not impact compliance.<sup>20</sup> No specific concerns are given by the submitter, but the Parties' note that their SAP and electronic shelf label systems will be unaffected by the Proposed Transaction. The Parties are willing to answer any questions the Commission may have on this topic.

**Lisa Asher**

**The market should be defined as the retail supply of groceries and exclude the co-ops' wholesale businesses which are immaterial to the overall revenue generated by the supermarkets. Including wholesale would only be an attempt to dilute the co-ops claimed market share.**

- 83 The purpose of this statement is unclear, but the Parties are comfortable with defining separate retail and wholesale (comprising separate regulated and commercial) markets – see the clearance application for more detail.

**States Ernie Newman's view (subsequently revised) that there appears to be cartel conduct between the co-ops. What has potentially been coordinating behaviour towards no competition and harmonisation against Woolworths should not be grounds for the two co-ops to merge.**

- 84 Note that Ernie Newman's submission was revised to remove this claim. On the business model more generally, see above from 41.

**The market power and consequent bargaining power that would occur from a merged entity, could be used to bargain harder with suppliers for concessions, and increase prices to shoppers, as there is only one competitor, Woolworths.**

- 85 This concern appears to relate to market power on both the retail and acquisition side. The merged entity would not hold greater retail market power than the co-operatives separately, for the reasons set out above at 48.
- 86 The Proposed Transaction would also not result in any lessening of competition for the acquisition of grocery products, for the reasons set out above from paragraph 1.
- 87 For completeness, and although it is not directly relevant to the merger clearance process, for the reasons set out elsewhere in this submission the Parties disagree with the statement that there is a lack of competition and incentive to compete.

---

<sup>20</sup> The Parties further note that some Four Square stores fall below the store size that triggers the unit pricing requirements.

***The value share of private label in NZ in 2022 was 13% (based on data from Food Ticker), reflecting ~\$3b of an estimated \$19b sales in stores in 2023 (based on data from figure.nz).***

***If the co-ops merge, the range across islands will be harmonised, and competition from small suppliers in the South Island is at risk, further lessening competition.***

***As detailed in the NZFGC supplier survey submitted to the Commission in 2021 (Supplier Survey), FSNI has requested brands that are already ranged to "tender" lowest pricing to remain in their range as it rationalises brands. Private label only needs to be cheaper than the cheapest brand and this concentration in categories can also lead to price creep of private label as it is indexed to other brands and across retailers. Therefore, with less competition, prices can go up.***

***The deliberate removal of brands unwilling to meet FSNI's margin expectations will be extended to the South Island if the merger goes ahead, impacting competition.***

- 88 As noted above, the Proposed Transaction will have no impact on competition as it concerns private label offerings, as private label activities are already carried out jointly by the Parties. As such, there is already potential for the same range to be present across both islands. However, private label range does vary in different locations, based on local consumer preferences. There is no incentive (nor plan) to change this feature following the Proposed Transaction, as the Parties' incentives will continue to be to optimise its offering for consumers across New Zealand.
- 89 The submitter is correct to identify that a reduction in competition for the supply of particular grocery products could lead to higher grocery prices. The Parties are strongly incentivised to avoid a reduction in competition among suppliers (e.g. this was a key reason private label products were introduced), as they ultimately suffer in terms of the prices they pay for products, and the depletion of their offering to consumers. See also above from paragraph 1. It is also correct that the Parties' private label offering is required to compete with other suppliers to be ranged (as described above) – private label products are not "indexed to other brands and across retailers", rather they must compete with branded products on price.
- 90 Further information on private label issues is set out above from 34.
- 91 Information on the position of smaller suppliers is set out above from 8.
- 92 Information on centralised buying is set out above from 22. It is incorrect to describe centralised buying as "the deliberate removal of brands unwilling to meet FSNI's margin expectations". Rather, centralised buying is focused on understanding the needs of customers, delivering a range that meets those needs and offering value in a cost-effective manner. Further, centralised buying is a feature of category reviews and procurement in both the factual and the counterfactual, given FSSI is progressing a similar practice to FSNI and intends to continue to do so absent the Proposed Transaction.
- Profitability***
- 93 The Parties disagree with much of the discussion regarding profitability. However, as no merger effect is identified the Parties do not discuss the issue further.



**Profitability has been achieved through (i) obtaining higher concessions from suppliers (captured in the supplier survey), (ii) the shift of paid/off location funds instore to head office as a % of "Retail Sales Value" to then be redistributed back to members and (iii) rationalising brands on shelf by banner referred to as a "tender", have contributed towards higher margins or rebates given by suppliers in exchange for remaining on shelf. The submission notes that the merger will lessen competition as the increase in market power would harmonise this practice throughout both islands and remove supplier competition further.**

94 The Parties consider this part of the submission mis-characterises their buying practices. In any event, the effect of the Proposed Transaction on buying practices is set out above at 8 and 22.

**FSNI is using Dunnhumby to help grow its profit, through use of customer data. Customer data can be commercialised by selling some of it to suppliers who are willing to pay, and internally using it to increase revenue and profit.**

95 The Parties consider this submission mis-characterises their practices in terms of ranging, retail price and margin decisions. Further, no merger effect is identified with respect to the Parties' use of Dunnhumby.

**PAK'nSAVE and New World pricing bookends Woolworths New Zealand pricing. With Foodstuffs bookending Woolworths with two banners, and relativity in pricing enforced at supplier level to pay for differences, there's no incentive for the retailer to compete on price, only to hold relativity and margin. The merger will lessen competition as the increase in market power would harmonise this practice throughout both islands and remove supplier competition further.**

96 This is incorrect. FSNI and FSSI (through both the PAK'nSAVE and New World banners) compete hard with Woolworths on price – see, for example, [ ]. This competition demonstrates that the co-operatives are incentivised to compete on price, which will not change as a result of the Proposed Transaction.

97 As to the concern regarding coordination arising from the harmonisation of procurement practices, see 32. As to the impact on suppliers see from paragraph 1.

**Suppliers are also being asked to pay FSNI head office a % of its sales to them for the stores to stock their own shelves, which is a standard cost of a grocery retailer's business. To agree to give the retailer a merchandising term either requires an increase in list price for the supplier or move of merchandising labour as a cost fully to the retailer, and the redundancy of the suppliers merchandising staff to fund this.**

98 No merger effect is identified. This part of the submission also mis-characterises the relationship between FSNI and suppliers.

**The 2013 merger did not result in the outcomes claimed pre-merger (based on a news article extract).**

99 Points regarding the 2013 merger (and the relevance to the current process) are set out above at 63.

**The Commission should retrospectively review the merger which created FSNI and require a divestment of PAK'nSAVE.**

100 This concern is outside the scope of the current merger clearance process. [

].

**Food and Grocery Council New Zealand (NZFGC)*****The proposed merger removes the potential option of more competition.***

101 As noted elsewhere, the Parties do not consider the Proposed Transaction removes the potential option of more competition, in short because there is not competition between them and such competition is not likely to arise in any realistic counterfactual – see from 44 above.

***NZFGC members have a number of concerns regarding the merger, including that:***

- ***the merger would be a three-to-two on the buy-side. This will contribute to concentration in wholesale supply. More powerful wholesalers enhance wholesale market power and make market entry less likely.***
- ***The merger will increase the co-operatives' market power on a national level. The concentration of buyer power would lead to greater price pressure, placing members at risk, and a reduction in the supplier base which could lead to reduced choice for consumers.***

102 No additional evidence is presented as to this proposition. The Parties have set out their views on why the Proposed Transaction would not reduce competition on the buy side in the clearance application. The Houston Kemp report at **Appendix B** provides the appropriate economic framing for the Parties' experience, supporting that a "three-to-two" is not a fact-based characterisation of the way buying occurs, and that there would be no lessening of competition.

103 The Parties acknowledge suppliers' experience of dealing with two co-operatives separately, and that that would amalgamate into one. From the Parties' experience and based on the economic evidence, that change should not give rise to any material competition effect. In addition, the Parties anticipate the merger would result in cost savings for suppliers.

***The status quo as a valid counterfactual is concerning. NZFGC considers it is necessary for the Commission to investigate all relevant contracts, agreements and understandings.***

104 In the Parties' view this concern is unfounded. Much of the testing of this issue takes place between the Commission and the Parties – given it is internal to FSNI and FSSI it is commercially sensitive - but the position is described at a high level from 43.

***There is no evidence that any claimed efficiencies by the merger will be "passed on" to consumers. It will be harder for suppliers to negotiate pass through of price reductions and specials for consumers.***

105 Information relating to the likelihood that merger benefits are shared with consumers is set out above at 60 as well as in the clearance application.

106 It is not clear the basis on which it will be harder for suppliers to negotiate pass-through of price reductions and specials specifically. But in the Parties' view, and based on their experience, competition in relation to the acquisition of groceries will not be lessened by the Proposed Transaction and so there should be no meaningful effect on suppliers' ability to negotiate. See in particular, from 1 above, and the Houston Kemp report at **Appendix B**.

**While it may not appear likely that individual stores, groups of stores, or even one of the Foodstuffs entities would exit to join a new entrant or start de novo, that may be due to current circumstances (which could change) and/or the existing arrangements between the parties (which as noted may be invalid and require full review).**

107 These possibilities do not form part of any realistic counterfactual – see from 44 above. Further, each co-operative has constitutional provisions and a protection trust structure which ensures that they remain owned by independent grocers. This structure is fundamental to the co-operatives, cannot be changed by the current members or trustees, and will be preserved throughout the merger. The protection trust structure prevents the outcome the submitter speculates about.

108 Even if these possibilities did form part of a realistic counterfactual, it is not clear they would represent a more competitive scenario than the status quo. Different ownership of Foodstuffs stores in specific local areas would merely replace Foodstuffs and not add a market participant.

**The merger can be expected to increase barriers to entry which can be expected to significantly reduce the likelihood of market entry/expansion, particularly as both co-ops appear to be actively expanding, with big rollouts of new stores and distribution centres.**

109 The Parties assume that, in making this point, the NZFGC is suggesting that the Parties' expansion through new stores and distribution centres is the source of the increase in barriers to entry. The Proposed Transaction will not give rise to a change in the Parties' footprint in any local market, nor will it give rise to any change in the concentration of distribution infrastructure (which is island-based). As such, the Proposed Transaction is not capable of giving rise to any anti-competitive effect in these areas. Furthermore, the Proposed Transaction would not give rise to any changes in incentives associated with expansion decisions. As such, it can be expected that there would be no meaningful difference between the factual and counterfactual with respect to expansion decisions.

**It cannot be argued that there will be no impact on the volume of groceries acquired from suppliers, while also asserting that downstream there will be enhanced competition. This indicates that consumers will get no benefits.**

110 The Parties do consider that, to the extent they are able to lower prices for grocery products relative to their competitors, they may gain market share and therefore acquire a higher volume of grocery products. This would be a pro-competitive effect of the Proposed Transaction. It is discussed in more detail above from 69.

**NZFGC considers that the merger increases the risk of coordinated effects (accommodating behaviour) on the buy-side as the two RGRs will have (1) more similar costs structures; (2) the knowledge that suppliers have fewer options; (3) a greater ability to know the other main buyer's offer.**

111 This issue is refuted above at 32.

**There will be reduced viability of a third-party entrant, removing the option of breaking up the current arrangements where one entity could sell to a new entrant.**

112 This concern is unclear to the Parties, although they note that the merger cannot increase barriers to entry if it does not give rise to any material competition effect. See also 107 above regarding the Parties' protection trust structure.

113 The Parties are, of course, willing to answer any questions the Commission may have on it.

***While the range of regulatory reform may be hoped to assist, it is far too early to tell what difference it will make over time. The Parties seem to suggest that regulation will ensure no competition concerns. The NZFGC is concerned at the suggestion that regulation designed to unwind market structure issues will protect against further competition issues.***

114 This point mis-characterises the Parties' submissions – see above at 66.

***The proposed merger would be contrary to the achievement of the purposes and expectations in the GICA and of the Commissioner's role to effectively report on the state of competition when it could be shrinking by the year. The merger necessarily impacts the efficacy of the regulatory regime, by reducing the number of regulated entities and the importance of this for benchmarking.***

115 The Proposed Transaction would not reduce the number of regulated entities that are present in any geography. Put another way, only one of the Parties is in competition with the other regulated grocery retailer, Woolworths, in any geography. As such the Proposed Transaction should not impact benchmarking (regardless of whether doing so would be an anti-competitive effect), nor would it "shrink" the state of competition. If anything, it could be simpler to administer the regime to deal with two regulated grocery retailers rather than three.

***The NZFGC has a number of concerns regarding compliance with the Grocery Supply Code.***

116 Issues relating to current Code compliance are separate from and unaffected by the Proposed Transaction. They are appropriately dealt with through direct engagement between retailers and suppliers, and the Commission.

***In terms of wholesale supply issues, the Commission should consider the absence of existing competition between Trent's and Gilmours.***

117 This issue is unclear to the Parties. The Parties have described the business model of Trent's and Gilmours in the clearance application and are willing to answer any further questions on it.

***Supermarkets owning wholesalers has led to market consolidation and higher pricing for all consumers. Further concentration with the proposed merger cannot logically lessen market consolidation or reduce pricing for customers.***

118 No evidence is given as to how supermarkets' ownership of wholesalers has led to market consolidation and higher pricing and the Parties do not consider this is correct. In any event, the Parties' wholesalers do not compete with the retailers. They primarily focus on foodservice customers, there is little overlap with supply to retailers and the Proposed Transaction will not result in any concentration.

***In terms of regulated wholesale supply, the merger would reduce access seekers' options from three to two. The merger would also frustrate the regulatory regime, part of which is benchmarking.***

119 FSNI's distribution infrastructure enables it to offer wholesale access to North Island access-seekers, while FSSI's distribution infrastructure enables it to offer wholesale access to South Island access-seekers. For these customers the Proposed Transaction would not reduce the number of options.

120 For national customers, the Proposed Transaction should enable a more coherent offer by combining the Parties' existing offers into one national offer, which is more competitive with Woolworths' national offer, thus improving competition to supply such customers.

***A merger would not only consolidate bricks and mortar, but brand buying power, particularly for Foodstuffs' private label, because the proposed merged entity will represent close to 60% of the grocery sector. Deranging to accommodate this leaves consumers with less choice. Further effects would include a loss of benchmarking and options.***

- 121 The Proposed Transaction would not consolidate brand buying power for private label, as private label is already carried out by a jointly-owned enterprise, FOBL. As such, there can be no "deranging to accommodate" this change. The harm associated with benchmarking and "options" is unclear, but the Parties are willing to answer any questions the Commission may have about it.

***Currently, both co-operatives may issue tenders for private label products that suppliers can choose to negotiate either for supplying to both or either co-operative. This will possibly not be available under the proposed merger, and NZFGC is surprised that the SOPI does not touch on the potential impact in private label.***

- 122 This concern mis-characterises the process for private label tenders, which are carried out by FOBL, and not separately by each Party. The Proposed Transaction is not expected to have any meaningful effect on this process.<sup>21</sup>

***The proposed transaction will result in the lessening of competition in relation to the retail supply of groceries. This is because:***

- ***consolidation/greater concentration structurally upstream would increase barriers to entry, and***
- ***greater centralisation could be expected, particularly if the merged entity were listed on a stock exchange or sold in its entirety.***

- 123 The meaning of "structurally upstream" is unclear, but the Parties do not consider the Proposed Transaction would give rise to consolidation that could cause a lessening of competition in relation to the retail supply of groceries. The consolidation of co-operative-level decision-making will not change any incentives with respect to competition in particular geographic markets.

- 124 Listing the merged entity on a stock exchange or selling it in its entirety is not a realistic counterfactual (nor would it have a material effect on competition) – see also above at 107 for further information regarding the Parties' protection trust structure. The rationale for the Proposed Transaction has been stated publicly, and the Commission has the ability to test that the Parties have accurately described it.

***NZFGC considers that existing competitors and prospective competitors entering selected locations would be capable of impacting FSSI or FSNI but not the entire Foodstuffs network. The geographic impact is important because FSSI deals with significantly more distant and less populous locations than FSNI.***

- 125 The merger effect is unclear. The submitter appears to acknowledge that retail competition can be local, which the Parties agree with. However, the Parties disagree that FSNI does not operate in low-population areas. Regardless, local retail competition would be unaffected by the Proposed Transaction.

---

<sup>21</sup> There may be limited instances in which the Parties negotiate separately for the supply of private label products. In relation to [ ]. The points relating to suppliers would apply in these instances – see paragraph 1 and **Appendix B**.

**Greater scrutiny is required considering the whole supply chain. The upstream aggregation will have downstream impacts. This could include, aggressive rollout of new stores, increased private label products, greater ability to resist regulatory influence as a result of greater resources and greater likelihood of "creeping" acquisitions).**

126 The lack of impact on the roll-out of new stores is addressed above from 109.

127 The lack of impact on private label is addressed above at 34 and 88.

128 It is not clear how the Proposed Transaction would bestow greater ability to resist regulatory influence. In the Parties' experience, New Zealand policymakers and regulators are well-equipped to carry out policy, regulation and enforcement, independently and effectively, irrespective of the resources of the subject of these steps. Furthermore, both Parties have cooperated with all regulatory processes and investigations, and are vigorously pursuing compliance with all new regulatory interventions, and there is no reason to expect that to change. The Parties expect the level of scrutiny they are subject to would continue in the same vein following the Proposed Transaction.

**Conglomerate effects may need to be considered.**

129 These are addressed above at 74 and 77.

**The merger will make potential forced separation or divestiture more difficult (should a government decide it would be in the long-term consumer benefit).**

130 No physical store or distribution assets are being consolidated so the basis for this concern is unclear. See also below from 136.

**NZFGC surveyed its members, to which 70 suppliers responded. The results of this survey highlighted the following concerns:**

- **Differences in terms and negotiations: 96% say there are differences in the two co-operatives' 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.**

131 The effect on negotiations with suppliers, in terms of overall procurement practices and the ability of suppliers to do deals with individual stores and groups of stores, is discussed above at 8 and 22.

132 The response rate for the survey is not given, nor does the total number of members of NZFGC appear on its website, so it is not clear how representative this survey is. Further, no methodological information regarding the survey is given with the submission.

- **Increased market power: 71% believe the status quo of three RGRs assists negotiations more than the proposal. 77% think the merged entity could have an increased ability to depress prices paid to suppliers.**
- **Other impacts: 76% have concerns about impacts in other parts of the supply chain and/or greater costs being imposed on suppliers.**

133 Information and evidence addressing this concern is provided above from 1 and in the Houston Kemp report at **Appendix B**.

- **No consumer benefit: 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.**

134 Information and evidence addressing these concerns are provided above at 69 and 88.

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

135 The source of this concern is unclear, but the Parties consider the Proposed Transaction would not be likely to result in a substantial lessening of competition, which would therefore preclude impact on barriers to entry and expansion.

#### **Monopoly Watch**

**This is not a merger of supermarkets but a merger of three-to-two distribution networks. The consolidation of distribution centres would further stall the provision of capital and in doing so, increase barriers to entry.**

136 The Proposed Transaction would not result in any consolidation of distribution centres. Each Party owns distribution infrastructure in the island it serves, and it is necessary to have distribution infrastructure in each island in order to uphold a national retail footprint, so there is no scope for consolidation.

**The reason for the merger is to facilitate a sell down of existing equity. The merger will enable the co-operatives to alter their trust documents and articles of association to allow for the existing PAK'nSAVE operators to sell and pull-out capital from the business at existing valuations (i.e. sell out at full monopoly rent valuation).**

137 As noted above, the reason for the merger has been stated openly and publicly. In summary, it is to achieve cost reductions (including overhead costs and product costs), efficiency gains, increased agility and innovation and a more cohesive national offering, which would ultimately deliver better value for customers at the checkout. The Commission has access to relevant internal documents to test that the Parties have accurately described the rationale.

138 See above at 107 for further information on the Parties' protection trust structure.

**The strengthening of the two co-ops, including the consolidation of the distribution centres, will enhance the power of in-house brands, notably Pams (NZ's largest vertically integrated brand by revenue and market share).**

139 The Proposed Transaction would not result in any consolidation of distribution centres. In any event, it is not clear how consolidating distribution centres would enhance the power of in-house brands. The Proposed Transaction would have no meaningful impact on private label, as detailed above from 34 and 88.

**There is no market mechanism for any passing of benefits to consumers because there is no price competition in the market.**

140 The Parties' views on the incentives to share merger benefits with consumers are set out above at 66.

***The proposed merger significantly increases the barriers to entry for a third-party challenger e.g. Monopoly Watch considers that should a merger take place not 120 stores will need to be divested to create a third operator but 180.***

141 The submitter does not identify the source of the increase in barriers to entry for a “third party challenger”. But if the Proposed Transaction would have no adverse effect on competition, it follows it would not adversely impact barriers to entry and it is not necessary to offer divestments.

***The NZ Government and Commission should learn from the Australian experience, where Aldi was assisted to enter the market, which has not created competition or removed buyer market power.***

142 This concern appears to fall outside the scope of the merger clearance process.

***The data collection impact of the amalgamation and the network effects of this data create a much more serious barrier to entry, particularly with the potential for drone delivery and other ecosystems of further securing “adjacencies” in product sales.***

143 There are no current plans for drone delivery, with or without the Proposed Transaction, and it is not clear how this issue is linked with data effects (which are themselves unspecified). It is not clear to the Parties what is meant by “other ecosystems of further securing ‘adjacencies’ in product sales” but the Parties are willing to respond to any questions the Commission may have on this issue.

***Monopoly Watch disagrees that the wholesale grocery regime could assist a scalable third entrant. To solve the broken market its essential there is a level of DC competition. Monopoly Watch urges the Commission to ignore the marginal and inconsequential impact of the GICA in the evolution of real like for like third operator competition.***

144 This concern appears to fall outside the scope of the merger clearance process.

***A banner split of New World from PAK’nSAVE or Four Square is not the answer to the problem. Monopoly Watch would support the merger with specified remedies.***

145 An applicant for clearance may offer divestments where that would remedy an identified competition concern. The Parties’ position is that no lessening of competition can arise from the Proposed Transaction and therefore no divestment remedy need be offered. The Parties further note that some of the suggested remedies fall outside the scope of the clearance process.

#### **Northelia**

***The merger will intensify the perpetuation of the entities’ appropriation of brand scale and value chain from its suppliers.***

146 The Parties do not know what the appropriation of “brand scale” and “value chain” refers to. But the Parties’ view of the impact on suppliers is set out above at 1. See also the evidence provided in the form of the Houston Kemp report at **Appendix B**.

***The merger will diminish the opportunities for marginal suppliers in New Zealand, fracturing their ability to participate in the market.***

147 The Parties assume that “marginal suppliers” refers to smaller suppliers, as to which see above at 8 and 22.



**Other concerns that have been raised with the Parties, not dealt with above**

[

]

148 [

].

149 The Houston Kemp report at **Appendix B** provides evidence that any improvement in terms would not arise from a change that can be described as a lessening of competition. The uncertainty of outcome associated with any altered bargaining position is also reflected in the Parties' acknowledgement of the risks to their ability to achieving these benefits. The risks include, for example:

149.1 [

], or

149.2 [

].

150 In any event, product cost savings would only be a competition problem if they resulted in a reduction in competition. Otherwise, they are neutral, or pro-competitive if they result in lower retail prices than would otherwise prevail.

***For some products, there is a bargaining dynamic similar to a spot market, where Woolworths, FSNI and FSSI are key competitors to acquire a product. This dynamic is particularly evident in the case of product shortages.***

151 Based on the analysis in **Appendix B** (see paragraph 93), which accords with the Parties' experience, the key question is what are a particular supplier's options (and how would they be affected by the Proposed Transaction)? A product shortage does not, in general, affect the buyers with which a supplier may deal, and accordingly the position would not be different in these circumstances. Of course, the price may move in response to product availability, but the options affecting how that occurs would not typically alter.

***FSSI, as a smaller acquirer, could be considered to have a unique character and be a better option for suppliers seeking to get a "foot in the door".***

152 While FSSI is proud to foster new and innovative suppliers, it is not clear to the Parties the basis on which FSSI may be seen as a better option in this respect, and the Parties have not yet seen the evidence that has been presented to support it. (To the extent this proves to be the case, the Parties will be seeking to incorporate this advantage into the practices of the merged entity in conjunction with the Emerging Suppliers Forum launched by FSNI, given the Parties' focus on fostering new and innovative products.)

153 The Parties consider it may be the case that this impression has been formed by the fact that FSSI is less far along in rolling out its centralised buying practices and there is a perception (which the Parties do not consider accurate for the reasons

given elsewhere in this submission) that centralised buying will be less favourable to smaller suppliers. But this is not correct.

**APPENDIX B – HOUSTON KEMP REPORT**

Attached separately.