

## Statement of Unresolved Issues

### Life Health Foods / Chalmers Organics

4 May 2022

#### Introduction

1. On 23 December 2021 the Commerce Commission registered an application (the Application) from Life Health Foods NZ Limited (Life Health Foods) seeking clearance to acquire 100 percent of the assets of Chalmers Organics Limited (Chalmers) (the Proposed Acquisition).<sup>1</sup>
2. The Commission will give clearance if it is satisfied that the Proposed Acquisition will not have, or would not be likely to have, the effect of substantially lessening competition in a market in New Zealand.
3. Since registering the Application from Life Health Foods, we have published:
  - 3.1 a Statement of Preliminary Issues (SoPI) setting out the issues that we considered important at the start of our investigation in deciding whether or not to grant clearance;<sup>2</sup> and
  - 3.2 a Statement of Issues (Sol) setting out the potential competition issues that we had identified following our initial investigation.<sup>3</sup>
4. The SoPI and the Sol also provided background information about Life Health Foods and Chalmers as well as the industry in which they operate. These documents are available on our website, along with public versions of the submissions we received following publication of the SoPI and Sol.
5. This Statement of Unresolved Issues (SoUI) sets out the potential competition issues that have not been resolved to date and that we therefore continue to test. This is so that the merging parties and other interested parties have an opportunity to comment and provide us with additional information.

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<sup>1</sup> A public version of the Application is available on our website at: <http://www.comcom.govt.nz/business-competition/mergers-and-acquisitions/clearances/clearances-register/>.

<sup>2</sup> The SoPI dated 8 February 2022 is available at: [https://comcom.govt.nz/\\_data/assets/pdf\\_file/0031/276439/Life-Health-Foods-NZ-Limited-and-Chalmers-Organics-Limited-Statement-of-Preliminary-Issues-4-February-2022.pdf](https://comcom.govt.nz/_data/assets/pdf_file/0031/276439/Life-Health-Foods-NZ-Limited-and-Chalmers-Organics-Limited-Statement-of-Preliminary-Issues-4-February-2022.pdf)

<sup>3</sup> The Sol dated 23 March 2022 is available at: [https://comcom.govt.nz/\\_data/assets/pdf\\_file/0039/279759/Life-Health-Foods-NZ-Limited-and-Chalmers-Organics-Limited-Statement-of-Issues-23-March-2022.pdf](https://comcom.govt.nz/_data/assets/pdf_file/0039/279759/Life-Health-Foods-NZ-Limited-and-Chalmers-Organics-Limited-Statement-of-Issues-23-March-2022.pdf)

6. In reaching the preliminary views set out in this SoUI, we have considered information provided by the merging parties and other industry participants. We have not yet made any final decisions on the issues outlined below (or any other issues) and our views may change, and new competition issues may arise, as the investigation continues.
7. We invite interested parties to provide comments on the likely competitive effects of the Proposed Acquisition. We request that parties who wish to make a submission do so by **17 May 2022**.

### **The concerns we are testing**

8. In the Sol, we identified concerns that the Proposed Acquisition could lead to unilateral effects in relation to a national market for the supply of tofu to the major grocery retailers.<sup>4</sup> After further investigation we are still not satisfied that the Proposed Acquisition would not be likely to substantially lessen competition in this way.
9. In summary, this is because we are not satisfied that:
  - 9.1 the competitive constraint imposed by existing suppliers of tofu to the major grocery retailers is likely to be sufficient to constrain the merged entity;
  - 9.2 entry by new suppliers, or expansion of existing suppliers is timely, likely and sufficient in extent to constrain the merged entity; and
  - 9.3 major grocery retailers are likely to exercise countervailing power to constrain the merged entity.
10. We discuss these outstanding concerns in more detail below.

### **Process and timeline**

11. We have agreed with Life Health Foods to an extension of time until **31 May 2022** in which to make a decision.
12. The Commission would like to receive submissions and supporting evidence from Life Health Foods, Chalmers and other interested parties on the issues raised in this Statement. We request responses by close of business on **17 May 2022**, including a public version of any submission.

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<sup>4</sup> The major grocery retailers in New Zealand are Woolworths New Zealand (Woolworths NZ), Foodstuffs North Island, and Foodstuffs South Island. Woolworths NZ's retail banners are Countdown, FreshChoice and SuperValue; Foodstuffs North Island's retail banners are PAK'nSAVE, New World, and Four Square; Foodstuffs South Island's retail banners are PAK'nSAVE, New World, Four Square, Raeward Fresh, and On the Spot.

13. All submissions received will be published on our website with appropriate redactions. All parties will have the opportunity to cross-submit on the public versions of submissions from other parties by close of business on **24 May 2022**.
14. If you would like to make a submission but face difficulties in doing so within the timeframe, please ensure that you register your interest with the Commission at [registrar@comcom.govt.nz](mailto:registrar@comcom.govt.nz) so that we can work with you to accommodate your needs where possible.

### Industry background

15. The merging parties both supply a range of manufactured plant-based products. There is a growing range of plant-based products and all industry participants advised that the demand for these types of products, particularly those which are designed to be an alternative to meat, is growing rapidly. Whereas in the past these products appealed largely to dedicated vegetarian and/or vegan consumers, there is a growing number of 'flexitarian'<sup>5</sup> consumers who are looking to consume these products.<sup>6</sup> The different types of plant-based products currently available include:
  - 15.1 tofu;
  - 15.2 meat-alternative patties;
  - 15.3 meat-alternative sausages; and
  - 15.4 meat-alternative chicken.
16. Table 1 below outlines the main plant-based products supplied by Life Health Foods and Chalmers.
  - 16.1 Life Health Foods supplies its plant-based products under brand names including Bean Supreme, Alternative Meat Co. and Vegie Delights.
  - 16.2 Chalmers supplies its plant-based products under the brand names Tonzu and Zenzo.

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<sup>5</sup> Flexitarianism is a style of eating that encourages eating mostly plant-based foods while allowing meat and other animal products in moderation. It is more flexible than fully vegetarian diets.

<sup>6</sup> Commerce Commission interview with [ ]. Commerce Commission Interview with [ ]. Commerce Commission interview with [ ]. Commerce Commission interview with [ ].

**Table 1: plant-based products supplied by Life Health Foods and Chalmers**

Product	Life Health Foods	Chalmers
Tofu	✓	✓
Tempeh	-	✓
Meat-alternative patties	✓	✓
Meat-alternative sausages	✓	✓
Meat-alternative mince	✓	-
Falafel	✓	-
Jackfruit	✓	-
Meat-alternative chicken	✓	-
Meat-alternative bacon	✓	-

Source: Application

17. As indicated in Table 1, the plant-based products most relevant to the Proposed Acquisition are tofu, meat-alternative patties and meat-alternative sausages, as these are the products which both merging parties supply.
- 17.1 Tofu is made by coagulating soymilk and then pressing the resulting curds into solid white blocks of varying softness.<sup>7</sup> It can then be further processed – including flavouring or frying. It is typically used as an ingredient as part of a meal.
- 17.2 Meat-alternative patties are designed to be a substitute for animal protein patties and can be made from a variety of ingredients – some are made from predominantly “whole” ingredients, like legumes or vegetables, while others are increasingly being made with textured vegetable proteins. Similarly, meat-alternative sausages are designed to look and cook like those made from meat. Again, meat-alternative sausages can be made from a variety of ingredients.
18. Life Health Foods and Chalmers, as well as other suppliers of plant-based products, supply their products to consumers through a range of different wholesale and retail customers, although the extent to which each supplier uses particular wholesalers and retailers to supply end-consumers varies. The merged entity would supply products to:
- 18.1 the major grocery retailers<sup>8</sup>;
- 18.2 specialty food retailers such as health food stores and specialty Asian supermarkets;
- 18.3 food service providers such as food wholesalers as well as cafés and restaurants; and

<sup>7</sup> The Application at [5.13]. The softness of tofu depends on how much moisture is pressed out of it, for example, firm tofu is pressed more than silken tofu.

<sup>8</sup> As above, the major grocery retailers in New Zealand are Woolworths NZ, Foodstuffs North Island, and Foodstuffs South Island.

#### 18.4 home delivery service providers.<sup>9</sup>

### The relevant markets

19. We define markets in the way that we consider best isolates the key competition issues that arise from a merger. In many cases this may not require us to precisely define the boundaries of a market. What matters is that we consider all relevant competitive constraints, and the extent of those constraints. For that reason, we also consider products and services that fall outside the market, but which still impose some degree of competitive constraint on the merged entity.
20. When assessing relevant markets, we consider whether, in response to a price increase on products of interest by the merged entity:
  - 20.1 customers could easily switch to alternative products (known as ‘demand-side’ substitution); and
  - 20.2 suppliers of different products could easily, profitably and quickly switch to supplying the products of interest (known as ‘supply-side’ substitution).

### Our preliminary views of the relevant markets

21. We have not yet formed a final view on market definition. However, based on the information we have collected to date, we continue to be of the view that:
  - 21.1 tofu is in a separate product market to other meat-alternative products;
  - 21.2 the major grocery retailers constitute a separate customer market to other wholesale and retail customers.
  - 21.3 the geographic scope of all of the relevant markets is national; and
  - 21.4 the relevant functional dimension is the wholesale supply of these products.
22. We set out our reasons for our current approach to market definition below.

*Tofu is in a separate product market to other meat-alternative products.*

23. In the Sol, we considered that tofu is likely to be in a separate product market to other meat-alternative products.
24. In response to the Sol, Life Health Foods submitted that all plant-based meat-alternatives – such as mince, patties, sausages, tofu and tempeh – are substitutes for most end consumers who buy any of them and so the relevant product market should include all plant-based products (including tofu).<sup>10</sup> Life Health Foods submitted that:

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<sup>9</sup> These sales are usually made as a part of meal kits, such as My Food Bag.

<sup>10</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [3.4].

- 24.1 tofu is used in a variety of different meal occasions, resulting in a differing range of alternatives that could be used as a substitute for tofu;
- 24.2 tofu and plant-based meat alternatives are stocked in the same shelf location at major supermarkets and other retail outlets, and all compete for available shelf space;
- 24.3 there are high levels of cross shopping occurring with other plant-based protein segments and animal protein sources; and
- 24.4 because there are many more ‘flexitarian’ consumers than exclusively vegetarian or vegan customers, the major constraint on sales of plant-based foods (including tofu) is the price relative to animal protein.
25. Chalmers also considers that the relevant product market is wider than tofu due to demand side substitution with other products. In its view, aside from people with very special dietary needs, no consumers would have the same protein option at every meal, whether they are plant-based or not.<sup>11</sup>
26. To date, on the demand side, we have received mixed evidence about how consumers (shoppers and diners) buy and consume plant-based products and how closely substitutable different products are for each other. Many market participants advised us that consumer preferences for plant-based products are complex and, in some areas, fast-changing.<sup>12</sup>
27. We have received feedback that:
- 27.1 tofu is a traditional Asian food, which means there are some uses in which it will not have any appropriate substitutes;<sup>13</sup>
- 27.2 some major grocery retailers stock meat-alternative products and tofu in different sections of the store;<sup>14</sup> and
- 27.3 based on [ ], retailers do not consider tofu and meat-alternative products to be close substitutes.<sup>15</sup>
28. On the demand side, since publishing the Sol, we have not received any further evidence to change the views expressed in our Sol. We are therefore not currently satisfied that meat-alternative products (such as meat-alternative patties and meat-

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<sup>11</sup> Submission from Chalmers in response to Statement of Issues (4 April 2022) at 1-2.

<sup>12</sup> Commerce Commission interviews with [ ].

<sup>13</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>14</sup> Commerce Commission interview with [ ].

<sup>15</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ]; [ ] data from [ ] in response to Commerce Commission request for information.

alternative sausages) are a sufficiently close substitute for tofu.<sup>16</sup> This is primarily because:

- 28.1 while consumers often purchase, and eat several types of plant-based products, this, in itself, does not indicate whether these products are sufficiently close substitutes that consumers would switch between if the relative price of one of the products increased; and
  - 28.2 while it may be possible to use firm tofu as a substitute for meat-alternative patties or sausages in certain situations, it may not be realistic to use softer or silken tofu, and vice-versa. For example, it is unlikely that meat-alternative sausages could be substituted for tofu in a traditional Asian meal.
29. On the supply side, in the Sol, we identified that most suppliers cannot easily switch production between tofu and meat-alternative products (such as meat-alternative patties and meat-alternative sausages).
30. Life Health Foods did not submit on this in its response to the Sol, but in the Application it noted that the same equipment can be used to manufacture a range of different meat-alternative products, and there are no significant barriers to switching production between types.<sup>17</sup>
31. We understand that, while many suppliers are able to switch production between meat-alternative patties and meat-alternative sausages (and other meat alternative products), most suppliers cannot easily switch production between tofu and meat-alternative products (such as meat-alternative patties or meat-alternative sausages).<sup>18</sup>
- 31.1 Tofu uses different equipment and processes than meat-alternative patties and meat-alternative sausages.
  - 31.2 Tofu uses soybeans as its main input, whereas other plant-based products can use a variety of inputs.<sup>19</sup> Other than the merging parties, we are not aware of producers of meat alternative sausages and patties that use tofu as a key ingredient.<sup>20</sup>
  - 31.3 Suppliers said they would have to make significant investments in new capital, processes and staff to switch production between tofu and meat-

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<sup>16</sup> Commerce Commission interview with [redacted]. [redacted] data from [redacted] in response to Commerce Commission request for information.

<sup>17</sup> The Application at [5.34].

<sup>18</sup> Commerce Commission interview with [redacted]. Commerce Commission interview with [redacted]. Commerce Commission interview with [redacted].

<sup>19</sup> Commerce Commission interview with [redacted].

<sup>20</sup> Chalmers advised that it is the only producer of meat-alternative sausages that have tofu as the main ingredient although we also understand that Life Health Foods' meat-alternative sausages also include tofu as an ingredient. Commerce Commission interview with Chalmers [redacted].

alternative products such as alternative patties and meat-alternative sausages.<sup>21</sup>

32. For these reasons, we continue to consider that tofu and other meat alternatives are not closely substitutable on the demand or supply sides, and vice versa. Therefore, our current view remains that tofu is in a separate product market from other meat alternatives.
33. In the Sol, we considered that it is appropriate to consider plant-based meat-alternatives (excluding tofu) to constitute its own product market. Our view has not changed, and we also consider that the Proposed Acquisition would not be likely to raise competition concerns in this area if we were to define narrower markets for plant-based meat alternatives (excluding tofu) by type. We therefore do not consider it necessary to undergo any further competition assessment for plant-based meat-alternative (excluding tofu) markets in this SoUI.
34. In its submission in response to the Sol, Life Health Foods submitted that the merging parties overlap in only one tofu product format: the firm tofu block. We have considered whether the different formats of tofu could form their own discrete product markets. Life Health Foods listed the four main formats of tofu as:
- 34.1 firm tofu block, which is supplied to major grocery retailers by several suppliers in addition to Life Health Foods and Chalmers;
  - 34.2 marinated tofu block, of which Life Health Foods is the only manufacturer that supplies this under its own label;<sup>22</sup>
  - 34.3 marinated tofu cubes, which only Chalmers currently supplies; and
  - 34.4 soft or silken tofu, which neither of the merging parties currently supply.
35. There appears to be little difference in the manufacturing processes to produce the different types of tofu, such that it is sufficiently easy to switch production between them, and so we consider that it is appropriate to include them all in a broad market for tofu.

*Functional and geographic dimensions*

36. As indicated in the Sol, consistent with the submissions in the Application, we consider:

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<sup>21</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ]; Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>22</sup> Woolworths does supply marinated block tofu under its Macro label. As discussed further below, this tofu is manufactured for Woolworths NZ [ ].



- 36.1 the functional dimension of the relevant markets is for the wholesale supply of the relevant product as suppliers supply wholesale customers, and not end consumers;<sup>23</sup> and
- 36.2 the relevant markets are likely to be national because the merging parties supply all customers on a national basis from central distribution bases.<sup>24</sup>

*The major grocery retailers are in a separate market to other customers*

37. In the Sol, we considered that competition to supply major grocery retailers should be assessed separately from competition to supply all other customers such as specialty retail stores, foodservice providers and home delivery service providers.
38. This was because we had received feedback that the major grocery retailers have requirements that only some suppliers can readily meet.<sup>25</sup> In contrast, it appeared that foodservice and specialty stores typically apply lower requirements on suppliers compared to major grocery retailers, meaning that more suppliers can supply them.
39. The evidence received to date indicates that only larger, and more efficient, tofu suppliers can supply the major grocery retailers on a scale required to compete effectively with one another. This means that supermarkets may have a different set of alternatives to other retailers, leading us to the view we expressed in the Sol, that competition to supply the major grocery retailers is separate from other customers.
40. In response to the Sol, Life Health Foods submitted that the customer dimension of the market should comprise the national supermarket chains, Asian supermarkets, speciality food stores and local food retailers. In its view, a separate market for major grocery retailers is inconsistent with the facts and contrary to commercial common sense.<sup>26</sup> Life Health Foods submitted that:<sup>27</sup>
- 40.1 while there might be the potential for separate customers market for “western” products, the situation is reversed for Asian products such as tofu. Tofu is a traditional component of East Asian and Southeast Asian cuisines so it should not come as a surprise that Asian supermarkets stock a greater range of, and typically sell more, tofu than equivalent sized western supermarkets (such as those operated by the major grocery retailers).
- 40.2 the major grocery retailers stock a smaller range of tofu than Asian supermarkets, and many specialist retailers. Asian supermarkets are the leaders in the tofu category. It is the “western” supermarket chains which are the followers.

<sup>23</sup> The Application at [5.37]-[5.39].

<sup>24</sup> Commerce Commission interview with Life Health Foods [ ]Commerce Commission interview with Chalmers [ ]

<sup>25</sup> For example, see Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>26</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [3.6].

<sup>27</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [3.7], [3.9] and [3.10].

41. Chalmers submitted that the majority of retailers in New Zealand should fall in the same market; the only reason a retailer might not be considered as part of the relevant market would be if they did not stock tofu or at least tofu related products like plant-based patties and sausages.<sup>28</sup> In its view, not including Asian supermarkets in the same customer market as the major grocery retailers would be the opposite of the reality that tofu suppliers face because:

41.1 Asian supermarkets are the leaders in the supply of tofu market to and they stock a much larger and wider range of tofu and tofu related products;<sup>29</sup> and

41.2 [ ]<sup>30</sup>

42. Our current view is that there is little differentiation between the tofu products (and meat-alternative products in general) that suppliers supply to each different type of wholesale customer. For example, the same product types, in similar pack sizes, are supplied by the merging parties to major grocery retailers and all other customers including Asian supermarkets.<sup>31</sup>

43. However, feedback from smaller tofu suppliers and the major grocery retailers indicates that the requirements to supply Asian supermarket or other foodservice customers do appear to be different than for the major grocery retailers.<sup>32</sup>

44. In particular, tofu suppliers we have spoken to have indicated that there are limited barriers to them supplying tofu to any Asian supermarket or other foodservice customers compared with supplying the major grocery retailers.

45. However, other than Life Health Foods and Chalmers, all the domestic tofu suppliers we have spoken with advised that the major grocery retailers make significantly greater demands on them than other customers do. Suppliers said that to achieve ranging at many of the major grocery retailers' stores they would need larger transportation and logistics operations than are needed to supply other customers. Suppliers also said that the major grocery retailers demand lower wholesale prices and more support with promotions and marketing than the suppliers could profitably provide in their current states. As a result, the other domestic suppliers said they cannot realistically achieve widespread ranging with the major grocery retailers with

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<sup>28</sup> Submission from Chalmers in response to Statement of Issues (4 April 2022) at 7.

<sup>29</sup> Submission from Chalmers in response to Statement of Issues (4 April 2022) at 8.

<sup>30</sup> Submission from Chalmers in response to Statement of Issues (4 April 2022) at 8.

<sup>31</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>32</sup> For example, see Commerce Commission interview with [ ]; Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

their existing equipment and infrastructure.<sup>33</sup> We were told that the cost to overcome these barriers for some suppliers is high.<sup>34</sup>

46. We have also received feedback from major grocery retailers that they would prefer to acquire supply of tofu from a small number of suppliers, as this will allow them to promote their offering more easily.<sup>35</sup> This requires larger volumes of tofu to be supplied to the major grocery retailers compared to other customers.
47. The lower volume requirements of specialty retailers makes it easier for smaller suppliers to supply these retailers on a store-by-store basis. Additionally, specialty retailers are able to acquire supply from several suppliers if desired, since they would not face the same logistical challenges (in terms of maintaining relationships with suppliers) that the major grocery retailers would face in the same scenario.
48. Further evidence is set out in the confidential Attachment.
49. Currently, both the major grocery retailers supply tofu under their private labels, and so this could be another route for suppliers to service the major grocery retailers.
  - 49.1 Foodstuffs supplies tofu under its Pams label. The tofu is manufactured for Foodstuffs by [ ].
  - 49.2 Woolworths NZ supplies tofu under its Macro label. The tofu is manufactured for Woolworths [ ].
50. However, much like supplying branded tofu products into the major grocery retailers, supplying private label tofu would require expansion in a way which is not required in order to supply other customers. The Foodstuffs entities and Woolworths provided feedback on the ability of existing suppliers of tofu to meet their requirements for supplying tofu under their private labels. Further evidence is set out in the confidential Attachment.
51. In our view, it appears that some existing tofu manufacturers would need to make significant investment in their infrastructure, particularly in their production capacity, to be able to be considered a genuine alternative supplier of tofu to the major grocery retailers.
52. However, in order for a tofu manufacturer to undertake such investment, the tofu manufacturer must be sufficiently confident there will be enough demand for the product to make it worthwhile. We assess the likelihood of this investment and/or expansion occurring in the competition assessment below.

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<sup>33</sup> For example, see Commerce Commission interview with [ ]; Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>34</sup> For example, see Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>35</sup> Commerce Commission interview with [ ].

53. We therefore continue to consider that it is appropriate to consider the major grocery retailers to be in a distinct market from all other customers, particularly, because it appears that they have fewer options meeting their requirements than specialty retailers.

#### **Current view of the relevant markets**

54. Based on the information we have collected to date, we consider that there are separate national markets for the wholesale supply of:
- 54.1 tofu to major grocery retailers; and
  - 54.2 tofu to specialty retail stores, foodservice customers and home delivery providers.
55. As previously mentioned, we are satisfied that the Proposed Acquisition is unlikely to raise competition concerns in the following markets, and as such, do not consider them again in this SoUI:
- 55.1 plant-based meat-alternatives (excluding tofu) to major grocery retailers; and
  - 55.2 plant-based meat-alternatives (excluding tofu) to specialty retail stores, foodservice customers and home delivery.
56. We seek submissions on our current views of the relevant markets. In particular, we invite submissions on:
- 56.1 whether tofu is likely to be in a separate product market to other meat-alternative products; and
  - 56.2 whether the major grocery retailers fall within a separate customer market to other customers, such as specialty retailers.

#### **With and without scenarios**

57. Assessing whether a substantial lessening of competition is likely requires us to:
- 57.1 compare the likely state of competition if the Proposed Acquisition proceeds (the scenario with the merger, often referred to as the factual) with the likely state of competition if it does not (the scenario without the merger, often referred to as the counterfactual); and
  - 57.2 to determine whether competition is likely to be substantially lessened by comparing those scenarios.
58. With the Proposed Acquisition, Life Health Foods would acquire the business and assets of Chalmers. Our current view is that the most likely counterfactual is a continuation of the status quo, with Chalmers continuing to operate independently of Life Health Foods.

### **Competition assessment: unilateral effects – relevant tofu markets**

59. Horizontal unilateral effects arise when a firm merges with, or acquires, a competitor that would otherwise provide a significant competitive constraint (particularly relative to remaining competitors) such that a market participant can profitably increase prices above (and/or reduce quality below) the level that would prevail without the merger.
60. In markets where products differ from one another (known as ‘differentiated markets’), some products will be closer substitutes and compete more vigorously with each other than others. Unilateral effects are therefore more likely to arise where the products produced by the merging parties are relatively similar.
61. For the same reasons as set out in the Sol, we are currently satisfied that the Proposed Acquisition would not be likely to substantially lessen competition in the supply of tofu to specialty retailers (such as Asian supermarkets), foodservice customers and home delivery providers. As indicated in the Sol, while both Life Health Foods and Chalmers supply tofu to some of these speciality customers, our investigation indicates there are several other suppliers of tofu who, collectively, would likely provide a constraint on the merged entity to speciality customers
62. However, the further inquiries we have made since the Sol continue to indicate that there are a more limited number of suppliers of tofu to the major grocery retailers than there are to speciality customers. For the reasons set out below, we are still not currently satisfied that the Proposed Acquisition would not be likely to substantially lessen competition in the market for the supply of tofu to the major grocery retailers.

### **The market for the supply of tofu to the major grocery retailers**

63. At this stage, the evidence we have seen indicates that Life Health Foods and Chalmers are the two largest suppliers of tofu to the major grocery retailers and there appear to be fewer tofu suppliers that can supply those retailers than there are for other customers.
64. For the reasons set out below, we are not currently satisfied that the Proposed Acquisition would not be likely to substantially lessen competition for the supply of tofu to the major grocery retailers.

### *The merging parties appear to be each other’s closest competitor*

65. In the Sol, we considered that Life Health Foods and Chalmers are each other’s closest competitor for the supply of tofu to the major grocery retailers.
66. In its submission in response to the Sol, Life Health Foods stated that it and Chalmers are not each other’s closest competitor. Rather, it considers that the merging parties are just two suppliers of plant-based product who complete closely with a range of other plant-based product manufacturers.<sup>36</sup> Further, even in a product market

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<sup>36</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [2.3]-[2.4].

limited to tofu, Life Health Foods does not consider that the merging parties are each other's closest competitor.<sup>37</sup> For example, it noted that there are four types of tofu and there is only overlap in one of these types – firm tofu block.

67. We still consider the merging parties to be each other's closest competitors, as the vast majority of tofu sold through supermarkets appears to be firm block tofu.<sup>38</sup> Additionally, internal substitution data<sup>39</sup> indicates that the types of tofu supplied by the merging parties are closely comparable to one another, and that the Proposed Acquisition would remove a significant competitive constraint for the merged entity.
68. Chalmers also submitted that it does not consider its closest competitor is Life Health Foods. Chalmers submitted that it competes closely with a growing number of non-meat protein suppliers, which include:<sup>40</sup>
- 68.1 both domestic and overseas manufacturers of tofu;
  - 68.2 domestic manufacturers of meat alternative products; and
  - 68.3 larger multinational manufacturers of meat-alternative products.
69. However, the evidence currently before us indicates that Life Health Foods and Chalmers are each other's closest competitor for the supply of tofu to the major grocery retailers. This competition would be lost as a result of the Proposed Acquisition. Our investigation has identified that:
- 69.1 Life Health Foods and Chalmers currently supply the vast majority of all tofu, and in particular, firm block tofu sold by the major grocery retailers.<sup>41</sup> This is consistent with Life Health Foods' estimates;<sup>42</sup>
  - 69.2 with the exception of private label tofu products, it appears that other suppliers' tofu products are only stocked in between [ ] of the supermarkets of the major grocery retailers (as per Life Health Foods' submission), whereas the merging parties appear to be the only suppliers whose tofu products are stocked throughout the network of stores of the major grocery retailers,<sup>43</sup> and

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<sup>37</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [4.1]-[4.5].

<sup>38</sup> [ ] data provided by [ ] in response to Commerce Commission request for information; Commerce Commission interview with [ ].

<sup>39</sup> [ ] data provided by [ ] in response to Commerce Commission request for information.

<sup>40</sup> Submission from Chalmers in response to Statement of Issues (4 April 2022).

<sup>41</sup> The vast majority of tofu sold in New Zealand is firm block tofu. Commerce Commission interview with [ ]. Emails from [ ]; [ ]; and [ ] in response to Commerce Commission request for information.

<sup>42</sup> For examples, see Application at [6.22]

<sup>43</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [4.5].

69.3 both have brands with significant brand recognition and loyalty in the supermarkets of the major grocery retailers.<sup>44</sup>

70. We invite further submissions on how closely Life Health Foods and Chalmers compete to supply tofu to the major grocery retailers.

*Constraint from existing domestic suppliers of tofu*

71. In the Sol, we stated that we are not yet satisfied that competition from existing suppliers of tofu would provide sufficient constraint on the merged entity in supplying tofu to the major grocery retailers.

72. In response to the Sol, Life Health Foods and Chalmers both submitted that the merged entity would face vigorous competition in the supply of tofu from all existing meat-alternative suppliers.<sup>45</sup> In particular, Life Health Foods considers that domestic tofu manufacturers such as Evergreen Foodstuffs Limited, with its Hing's brand of tofu and ECLY Limited, with its Check brand of tofu, would compete vigorously with the merged entity. Life Health Foods submits that:

72.1 Hing's and Check branded tofu is supplied through both Asian supermarkets and the major grocery retailers;<sup>46</sup>

72.2 Asian supermarkets compete with the major grocery retailers, and the two national supermarket chains themselves recognise this constraint;<sup>47</sup> and

72.3 the barriers to expansion in supplying tofu to any customers are very low and it is not difficult for existing suppliers to increase the quantity and range of their tofu products. As such, tofu suppliers such as Hing's and Check are well placed to scale up supply of tofu more broadly into western supermarkets nationwide.<sup>48</sup>

73. Our investigation has identified several suppliers of tofu to speciality retailers, foodservice customers and home delivery providers, in addition to the merging parties.<sup>49</sup> Competing suppliers consider the quality and taste of their respective tofu products to be comparable to the tofu to supplied by the merging parties.<sup>50</sup> These suppliers include, but are not limited to:

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<sup>44</sup> For example, we received feedback that [ ], if one brand's tofu product is not available, customers will look to switch to another tofu product of the same brand, before switching to a comparable product from a different brand. See Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>45</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [2.2]-[2.5] and Submission from Chalmers in response to Statement of Issues (4 April 2022) at 4.

<sup>46</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [5.3]

<sup>47</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [3.8].

<sup>48</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [5.1] and [5.3].

<sup>49</sup> For example, although Chalmers is able to supply its tofu on a nationwide basis, it is not a leading supplier into specialty stores. On the other hand, local tofu suppliers are able to build relationships with local retailers on a store-by-store basis.

<sup>50</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

- 73.1 Evergreen Foodstuffs Limited (Hing's), a Wellington based manufacturer of tofu, soymilk and noodles who currently supplies products around the lower North Island region, to customers including Foodstuffs North Island and small cafés and restaurants;
- 73.2 ECLY Limited (Check), an Auckland-based food importer and distributor, which also has an outlet in Wellington. Check says it focuses on distributing Asian food products to Asian grocery stores within Auckland, although their tofu products can be found in selected major grocery retailers as well; and
- 73.3 Best Food Fresh Tofu Limited, an Auckland-based manufacturer of tofu, soymilk and rice noodles. It predominantly supplies Asian supermarkets in Auckland, but also supplies some major grocery retailers and stores outside the Auckland region.
74. Absent any expansion in the supply of tofu to the major grocery retailers, it does not appear that the level of constraint provided by these suppliers would likely be sufficient to constrain the merged entity post-transaction. This is because these suppliers' offerings in the major grocery retailers are limited to certain geographic areas and/or product ranges, such that they are unlikely to compete effectively with the merged entity.
75. While none of these suppliers indicated that they have significant constraints on their ability to expand their existing supply of tofu to speciality retailers, such as through Asian supermarkets,<sup>51</sup> they advised there are constraints on their ability to supply the major grocery retailers, which is why they currently have a very limited presence in these stores.
76. To date, the evidence before us indicates that, in order to provide a constraint on the merged entity in the supply of tofu to the major grocery retailers, existing tofu manufacturers would need to:
- 76.1 significantly increase their production capacity;
- 76.2 expand their range of tofu products supplied to the major grocery retailers; and/or
- 76.3 increase marketing to improve their brand recognition and equity.
77. Further evidence on the requirements and the ability of existing tofu manufacturers to expand to supply the major grocery retailers is set out in the confidential Attachment.
78. In our view, for an existing domestic tofu supplier to undertake the necessary investment to expand, the supplier must be sufficiently confident that there will be

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<sup>51</sup> For example, see Commerce Commission interview with [ ]; Commerce Commission interview with [ ]. Because of this, as outlined in the Sol, we are satisfied that the Proposed Acquisition would not be likely to substantially lessen competition for the supply of tofu to speciality retail stores, foodservice customers and home delivery providers.



enough wholesale demand for the product to make it worthwhile. We discuss the ability and incentives for domestic tofu manufacturers to expand further below.

79. However, given the feedback to date, we are still not yet satisfied that competition from existing domestic suppliers of tofu would provide sufficient constraint on the merged entity in supplying tofu to the major grocery retailers.
80. We invite further submissions on the extent to which existing domestic suppliers of tofu would impose a competitive constraint on the merged entity, including through an ability to expand their current supply of tofu to the major grocery retailers.

*Constraint from new entry and expansion from domestic suppliers*

81. In the Sol, we stated that we are not yet satisfied that competition from new entry and expansion would provide sufficient constraint on the merged entity in supplying tofu to the major grocery retailers. In particular, we noted that tofu manufacturers who only supply tofu into specialty stores, such as Asian supermarkets, would face the same constraints that the smaller existing suppliers to the major grocery retailers do when it comes to supplying the major grocery retailers.
82. Entry or expansion must be likely, as well as timely and of sufficient scale, before it could constrain the merged firm and prevent a substantial lessening of competition. The likelihood of entry or expansion depends on firms' assessment of the profitability of such entry or expansion.
83. In response to the Sol, Life Health Foods submitted that the barriers to entry and expansion for tofu and meat-alternative products are low. Life Health Foods asserted that:
  - 83.1 the significant number of new entrants into the supply of plant-based foods New Zealand, including local start-ups, existing food producers extending to plant-based and international players, illustrates that barriers to entry are low;<sup>52</sup>
  - 83.2 tofu is a growing segment within the plant-based category and any current or future market participants could choose to expand into this segment. Tofu manufacturing equipment does not carry significantly different investment requirements than other plant-based products;<sup>53</sup> and
  - 83.3 many new entrants initially supply Asian supermarkets or specialty retail channels, then in time selected Foodstuffs stores, before growing to nationwide supermarket representation. This is in fact consistent with Life Health Foods' and Chalmers' history, which both began in speciality retailers, and is also the case for other tofu suppliers such as Hing's and Check.

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<sup>52</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [6.1]-[6.2].

<sup>53</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [6.2]

84. Chalmers also submitted [ ]<sup>54</sup>
85. To date, all industry participants have advised that the production process to manufacture tofu is relatively simple.<sup>55</sup> Further, consistent with Life Health Foods' and Chalmers' submissions, the barriers to supplying tofu to specialty retailers, such as Asian supermarkets, appear to be relatively low. This indicates that that entry by smaller scale tofu manufacturers, who can then service local outlets in different parts of New Zealand, is likely to be relatively straightforward.
86. However, the evidence before us continues to suggest that a new entrant would face the same issues that the smaller existing suppliers of tofu do when looking to supply the major grocery retailers and achieve national ranging.<sup>56</sup> For example, potential suppliers noted that:
- 86.1 to be able to compete effectively with the merging parties they would need to achieve significant scale;<sup>57</sup>
  - 86.2 investing in achieving scale would be too risky, and too unlikely to make the required return on investment, to be attractive unless incentivised by a sufficiently large and guaranteed contract;<sup>58</sup>
  - 86.3 unlike most other domestic tofu suppliers, the merging parties offer a range of tofu products, as well as other meat-alternative products, which gives them an advantage when it comes to distribution<sup>59</sup> and during negotiations with the major grocery retailers;<sup>60</sup> and
  - 86.4 customers exhibit a high degree of brand loyalty.<sup>61</sup> This can result in entry and/or expansion not having the desired competitive effect of constraining the merged entity and could be unprofitable for the supplier.<sup>62</sup>
87. These issues appear to be the same whether the new entrant is:
- 87.1 a de novo entrant in the supply of tofu;

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<sup>54</sup> Submission from Chalmers in response to Statement of Issues (4 April 2022) at 6.

<sup>55</sup> For example, see Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>56</sup> For example, see Commerce Commission interview with [ ].

<sup>57</sup> For example, see Commerce Commission interview with [ ].

<sup>58</sup> For example, see Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>59</sup> For example, it can make it easier for them [ ].

<sup>60</sup> For example, see Commerce Commission interview with [ ].

<sup>61</sup> Commerce Commission interview with [ ].

<sup>62</sup> Email from [ ] to the Commerce Commission (2 March 2022). Commerce Commission interview with [ ].

- 87.2 an existing tofu manufacturer who currently only supplies tofu through specialty stores, or small volumes to the major grocery retailers; or
- 87.3 an existing supplier of meat-alternative patties or a similar plant-based product.<sup>63</sup>
88. We invite submissions on the extent to which new entry or expansion would be likely to effectively constrain the merged entity in the supply of tofu to the major grocery retailers.

*Constraint from entry or expansion of overseas-based suppliers of tofu*

89. In the Sol, we stated that we are not satisfied that competition from existing suppliers of tofu, whether they are domestic manufacturers or based overseas, would provide sufficient constraint on the merged entity in supplying tofu to the major grocery retailers.
90. In response to the Sol, Life Health Foods stated it does not regard parallel importing of other brands of tofu as likely, given that tofu is a chilled product, requiring close management of shelf life and product quality and integrity.<sup>64</sup>
91. Chalmers submitted that there is significant new trend of Asian manufacturers bringing their brands into the supermarkets operated by the major grocery retailers in New Zealand and this includes recent entry into Foodstuffs supermarkets from the Korean brand Jongga, which has occurred since Life Health Foods' application was registered.<sup>65</sup>
92. [ ], we understand that some of the tofu currently sold by the major grocery retailers is imported from overseas manufacturers. These products include tofu sold under the brand names Mori-Nu and Jongga.
93. Mori-Nu tofu is manufactured by Morinaga Nutritional Foods, Inc in the United States. Mori-Nu is a silken tofu which is not typically used in the same way as firm tofu. It is shelf-stable and it is typically not stocked in a chiller, unlike most other tofu. In our view, Mori-Nu's tofu is not a close competitor to the merging parties (which predominantly supply firm tofu).
94. Jongga tofu is manufactured by the Daesang Corporation in South Korea. We understand that Jongga branded firm tofu was first introduced in 2020 in some Foodstuffs South Island stores and currently accounts for [ ]% of sales into Foodstuffs South Island. While Jongga has achieved some success in some individual stores, we do not currently consider that it is likely to expand its supply of tofu to

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<sup>63</sup> Commerce Commission interview with [ ]. Commerce Commission interview with [ ].

<sup>64</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [7.17]

<sup>65</sup> Submission from Chalmers in response to Statement of Issues (4 April 2022) at 4.

such an extent to provide material constraint on the merged entity, given its low market share and limited ranging across the major grocery retailers.

95. We have contacted overseas-based manufacturers of tofu about their ability to export tofu into New Zealand to supply the major grocery retailers.<sup>66</sup> We did not receive any feedback identifying a likely entrant from overseas who would be able to effectively constrain the merged entity. Further evidence is set out in the confidential Attachment.
96. Based on the evidence currently before us, we are still not satisfied that competition from overseas-based manufacturers of tofu would provide sufficient constraint on the merged entity in supplying tofu to the major grocery retailers.
97. We invite further submissions on the extent to which imports of tofu would impose a competitive constraint on the merged entity in the supply of tofu to the major grocery retailers.

*Constraint from products outside of the market*

98. We are also considering the extent to which products from outside of the market for the supply of tofu to the major grocery retailers will constrain the merged entity. This can include meat-alternative products supplied to both the major grocery retailers and specialty retailers, as well as tofu supplied to specialty retailers.
99. In its submission in response to the Sol, Life Health Foods said that it would expect an increased level of switching to meat-alternative products if the price of tofu became too high.<sup>67</sup>
100. Since publishing our Sol, we have received data that indicates that meat-alternative products are not close substitutes for tofu.<sup>68</sup> We are therefore not satisfied that a sufficiently large number of consumers of tofu would switch to consuming meat-alternative products in response to a price increase of the merged entity's tofu products, such that the price increase becomes unprofitable for the merged entity.
101. We are also considering whether tofu supplied to specialty retailers would effectively constrain the merged entity.
102. In its submission in response to the Sol, Chalmers cited the Tai Ping supermarket in the mall at 277 Broadway, Newmarket (which is adjacent to a Countdown) as an example of how easily customers could shop for tofu at either Tai Ping or Countdown.<sup>69</sup>

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<sup>66</sup> The major grocery retailers indicated that they would consider acquiring supply of tofu from overseas-based tofu manufacturers. For example, see Commerce Commission interview with [ ]

<sup>67</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [2.3].

<sup>68</sup> [ ] data provided by [ ] in response to Commerce Commission request for information.

<sup>69</sup> Submission from Chalmers in response to Statement of Issues (4 April 2022) at 6.

103. While we acknowledge that, in the example cited in Chalmers' submission, there may be a higher degree of customer switching due to the closeness of the two stores (as well as other aspects such as a shared carpark for both stores), our current view is that for most consumers, tofu is unlikely to be considered a product that drives foot traffic to the point where a sufficient number of customers switch to purchasing tofu in specialty retailers, constraining the merged entity.
104. This is consistent with the Commission's findings during its Market Study into the retail grocery sector, that convenience is the most important driver of store choice, and most consumers prefer to shop at a major grocery retailer, no matter their shopping mission.<sup>70</sup>
105. Additionally, the number of specialist retailers that supply tofu, and therefore the level of constraint they provide, varies in different parts of the country. For example, Tai Ping operates a network of 11 Asian supermarkets, but is only located in the Auckland region.
106. We are not yet satisfied that the constraint provided by tofu supplied into specialty retailers will prevent a substantial lessening of competition in the market for the supply of tofu to the major grocery retailers.
107. We are, however, continuing to seek information regarding the volumes of tofu sold through specialty retailers, and the extent to which this could constrain the merged entity.

*Countervailing power of major grocery retailers*

108. A merged firm's ability to increase prices profitably may be constrained by the ability of certain customers to exert substantial influence on negotiations. Countervailing power exists when a customer possesses special characteristics which give that customer the ability to substantially influence the price that the merged firm charges.<sup>71</sup>
109. These characteristics can include the ability to self-supply, or sponsor entry/expansion. This is distinct from the ability to leverage existing options to secure better prices and/or terms of trade.
110. While customers may have a degree of countervailing power, a merger which results in the removal of a supplier that was an important alternative for that customer will usually reduce that customer's negotiating power. In that case, the customer's remaining countervailing power may be insufficient to constrain the merged firm effectively.<sup>72</sup>

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<sup>70</sup> Commerce Commission Final Report of Market Study into the retail grocery sector at [4.62].

<sup>71</sup> Commerce Commission *Mergers and Acquisitions Guidelines*, at [3.115].

<sup>72</sup> Commerce Commission *Mergers and Acquisition Guidelines*, at [3.116].

111. In the Sol, we stated that we were not satisfied that the major grocery retailers would be likely to exercise whatever countervailing power they may have in order to constrain the merged entity in the supply of tofu to them.
112. In response to the Sol, Life Health Foods submitted that the major grocery retailers would have significant countervailing power over the merged entity and this countervailing power would act as a significant constraint on the merged entity.<sup>73</sup> In its view, its assessment of countervailing power in regards to the supply of tofu is consistent with the conclusions of the recent Commerce Commission study into New Zealand supermarkets.<sup>74</sup> In particular, in its view, the major grocery retailers are able to:
- 112.1 make ranging decisions and shelf space allocations to provide preferential positioning for their own private label products;
  - 112.2 encourage entry and expansion of new and smaller players; and
  - 112.3 give more favourable treatment to its private label products.
113. Chalmers also submitted that the major grocery retailers would have significant countervailing buyer power, as discussed above, over the merged entity. It stated that:
- 113.1 the major grocery retailers are always seeking better pricing and competitive quotes to pressure the incumbent suppliers;<sup>75</sup> and
  - 113.2 the major grocery retailers control retail pricing and if the merged entity attempted to raise prices, they would just go to one of the many alternative manufacturers to source their tofu.<sup>76</sup>
114. In this instance, we are not satisfied that the major grocery retailers would have the requisite outside options for supply that would give them countervailing power. Specifically, we are not satisfied that they would be likely to:
- 114.1 sponsor new entry;
  - 114.2 give favourable treatment to their own brands; or
  - 114.3 make product selection choices in other categories
- in such a way as to effectively constrain the merged entity.

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<sup>73</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [1.2 (d)].

<sup>74</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [7.10]-[7.16].

<sup>75</sup> Submission from Chalmers in response to Statement of Issues (4 April 2022) at 11.

<sup>76</sup> Submission from Chalmers in response to Statement of Issues (4 April 2022) at 11.

### Sponsoring entry and expansion

115. As stated earlier, the major grocery retailers have certain requirements which suppliers must meet, and we have not yet been able to identify any supplier who could meet these in a manner that would sufficiently constrain the merged entity.
116. To date, we have received mixed evidence on the extent to which one, or all, of the major grocery retailers would be incentivised to exercise any countervailing power they might have. For example:
- 116.1 while the demand for tofu is growing, it is not a category which the major grocery retailers focus on to any large extent, and may be unlikely to drive foot-traffic through the supermarkets compared to other products,<sup>77</sup> such as bread or milk; and
- 116.2 while we do recognise the presence of private label tofu products, the merging parties are the two largest suppliers of tofu to both major grocery retailers. We are continuing to assess whether both the grocery retailers would be equally affected by the price of a wholesale cost increase.
117. In its submission in response to the Sol, Life Health Foods submitted that both it and Chalmers were able to expand because of encouragement from the major grocery retailers.<sup>78</sup> We received feedback from the major grocery retailers that if the price of tofu were to go beyond a certain point, this may encourage entry of new tofu suppliers, although we were [ ] new entry as set out in Life Health Foods' submission.
118. [ ] advised that suppliers can use its distribution network if they are able to meet certain conditions relating to throughput of product.<sup>79</sup> [ ] said they can facilitate relationships with individual stores, which could be helpful for smaller suppliers to obtain a presence in stores, and may necessitate a lesser investment in logistics and distribution.<sup>80</sup> However, this may not be enough to incentivise a new supplier to enter. We have received feedback from suppliers of tofu that the cost of using a major grocery retailer's distribution network is prohibitive.<sup>81</sup> Further, suppliers may have to supply several stores in order to reach the throughput requirements for a perishable product such as tofu. This would likely require significant expansion from existing suppliers.
119. As noted above, expansion would require both investment in infrastructure to manufacture the volumes of tofu required by the major grocery retailers, but also

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<sup>77</sup> Commerce Commission interview with [ ].

<sup>78</sup> Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [7.11].

<sup>79</sup> Commerce Commission interview with [ ];

<sup>80</sup> Commerce Commission interview with [ ]; Commerce Commission interview with [ ].

<sup>81</sup> Commerce Commission interview with [ ].

investment in marketing, logistics and branding. There is a high degree of brand loyalty within tofu<sup>82</sup> which could require significant effort to overcome. Thus, we are not satisfied that expansion of existing suppliers of tofu would be sufficient to constrain the merged entity. However, we are seeking more information to identify under which conditions this expansion could be profitable.

120. Further evidence is set out in the confidential Attachment.

#### Expanding or favouring private label

121. The major grocery retailers have introduced private label tofu products. It is possible that they can expand their product ranges in this space by introducing more SKUs, as has happened with the Macro brand in Woolworths Australia. We also received feedback that in the event of a wholesale price increase, the major grocery retailers may see it as an opportunity to build the strength of their private label products. This may involve passing on wholesale price increases to consumers to try to switch more consumers to private label products.

122. However, based on the evidence before us, we are not currently satisfied that the major grocery retailers would be able to preference their private label brands in a way that constrains the merged entity.

##### 122.1 Woolworths Macro brand

[ ]. We are continuing to investigate its [ ] performance and also the extent to which Macro-branded tofu could be used to resist price increases by the merged entity; and

122.2 Macro tofu sales appear to be [ ]. We are continuing to investigate the reasons for this. One potential explanation is that there is much more brand loyalty for tofu in New Zealand. This was identified as a barrier to entry for some overseas suppliers.<sup>83</sup> More broadly, we are also continuing to consider the effect that this brand loyalty has on the major grocery retailers' ability to constrain the merged entity through the use of private label products.

122.3 While Foodstuffs has recently launched its Pams tofu, which is now available in [ ]% of all Pak'n Save and New World stores nationally,  
[

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[

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<sup>82</sup> Commerce Commission interview with [ ].

<sup>83</sup> Email from [ ] to the Commerce Commission (2 March 2022). Commerce Commission interview with [ ].



].<sup>84</sup> We are continuing to consider the ability of suppliers to manufacture private label tofu on behalf of a major grocery retailer.

#### Product selection choices in other categories

123. We are also considering the ability of the major grocery retailers to respond to price increases of tofu by taking action in other markets, such as switching (or credibly threatening to switch) to suppliers of other products it acquires from the merged entity.
124. Life Health Foods and its associated companies produce several products other than tofu including meat-alternative sausages and patties, but also breakfast cereal, spreads, and alternative milk products.<sup>85</sup> However, any ability to respond to price increases might be limited if there is no direct trading link between the relevant entities.<sup>86</sup>
125. We invite further submissions whether major grocery retailers are likely to be incentivised to exercise any countervailing power they might have to constrain an increase in the price of tofu by the merged entity.

#### *Summary of our current views on unilateral effects in the market for the supply of tofu to the major grocery retailers*

126. Based on the evidence gathered to date, we are not satisfied that existing suppliers of tofu would provide sufficient constraint on the merged entity to replace the competition lost as a result of the Proposed Acquisition.
127. Further, given the feedback to date, we are still not yet satisfied that competition from:
- 127.1 existing domestic suppliers of tofu would provide sufficient constraint on the merged entity in supplying tofu to the major grocery retailers;
  - 127.2 overseas-based manufacturers of tofu would provide sufficient constraint on the merged entity via importing tofu for supply by the major grocery retailer; and.
  - 127.3 new entry and expansion would provide sufficient constraint on the merged entity in supplying tofu to the major grocery retailers.

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<sup>84</sup> Commerce Commission interview with [ ].

<sup>85</sup> Life Health Foods is owned by the same parent company as Sanitarium.

<sup>86</sup> Life Health Foods considers that, while Life Health Foods and Sanitarium have common owners, each is a separate legal entity and so Life Health Foods and Sanitarium supply different product categories under separate and unrelated trading terms, Submission from Life Health Foods in response to Statement of Issues (4 April 2022) at [9.1]-[9.2]. This is also in line with feedback we received from [ ].

128. In addition, we are still not yet satisfied on the extent to which a major grocery retailer might exercise countervailing power in a way that constrains the merged entity.

### **Next steps in our investigation**

129. The Commission is currently scheduled to make a decision on whether or not to give clearance to the proposed acquisition by **31 May 2022**. However, this date may change as our investigation progresses.<sup>87</sup> In particular, if we need to test and consider the issues identified above further, the decision date is likely to extend.
130. As part of our investigation, we will continue to identify and contact parties that we consider will be able to help us assess the issues identified above.

### **Making a submission**

131. We are continuing to undertake inquiries and seek information from industry participants about the impact of the Proposed Acquisition. We welcome any further evidence and other relevant information and documents that Life Health Foods or any interested parties are able to provide regarding the issues identified in this SoUI.
132. If you wish to make a submission, please send it to us at [registrar@comcom.govt.nz](mailto:registrar@comcom.govt.nz) with the reference 'Life Health Foods/Chalmers' in the subject line of your email. Please do so by close of business on **17 May 2022**.
133. All information we receive is subject to the Official Information Act 1982 (OIA), under which there is a principle of availability. We recognise, however, that there may be good reason to withhold certain information contained in a submission under the OIA, for example in circumstances where disclosure would be likely to unreasonably prejudice the commercial position of the supplier or subject of the information.

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<sup>87</sup> The Commission maintains a clearance register on our website at <http://www.comcom.govt.nz/clearances-register/> where we update any changes to our deadlines and provide relevant documents.

**Confidential Attachment**

**Feedback from suppliers on entry and expansion**

[

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*Requirements to supply tofu to major grocery retailers*

[

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*Ability to import tofu into New Zealand to supply the major grocery retailers.*

[

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**Feedback from major grocery retailers**

[

]

*Ability of existing suppliers of tofu to meet their requirements for supplying tofu under their private labels.*

[

[

]

]

*Ability to exercise countervailing power*

[

]