

National Association of Retail Grocers of Australia

NARGA

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INFORMATION PACK

	Page
1. About NARGA	2
2. Key aspects of NARGA's pro-competitive philosophy	3
3. Growing Major Chain Dominance and Market Power - The Problem	5
4. Trade Practices Reforms – Key NARGA proposals	6
5. Competition Policy Reforms – Key NARGA proposals	9
6. GST Compliance Costs – Key NARGA proposals	11
 Attachments	
1. Major Chains' Retail Grocery Market Shares 1999-2001	13
2. Australia's Retail Grocery Sales 1975-2001	14
3. Retail Grocery Market Shares – Overseas Comparisons	15
4. Grocery Trade Concentration in Asia	16
5. NARGA Member and Allied Organisations	17

PO Box W245 Westfield

Parramatta NSW 2150

Phone: (02) 9806 1915

Fax: (02) 9806 1910

Email: alanmckenzie@narga.com.au

Website: www.narga.com.au

1. About NARGA

The National Association of Retail Grocers of Australia (NARGA) is a federation of associations representing independent grocery retailers in each Australian State and Territory. They are:

- IGA Retail Network
- Food Retailers Association of New South Wales
- Master Grocers Association of Victoria
- Queensland Retail Traders & Shopkeepers Association
- WA Independent Grocers Association
- Small Retailers Association of South Australia
- Tasmanian Independent Retailers
- Canberra Small Business Council Inc.

NARGA is non-party political and represents more than 4000 independent grocery stores and supermarkets employing more than 50,000 people throughout Australia. NARGA's membership base is national, covering not only the major cities, but also rural and regional Australia, including many towns where the major supermarket chains are not represented. In these towns the local grocery store is the heart of the community providing vital services and employment opportunities. It is therefore vital that these stores are competitive so as to maintain a vibrant local economy where the money and benefits generated remain in and support the community.

NARGA is committed to improving the welfare and viability of its members and, in doing so, does not seek handouts or protection. Rather, NARGA seeks recognition of and a reduction in the compliance costs faced by small business, and the adoption of trade practices and competition policies that enable small business to compete vigorously in the marketplace.

NARGA is concerned to ensure that independents provide a competitive third force within the retail grocery industry to counter the market power of the two major supermarket chains, which already dominate the national grocery market. In order to be such a force, the independent sector must, when buying comparable quantities, be able to acquire its supplies at comparable prices to those obtained by the two major supermarket chains. In addition, independents must not be strategically targeted by below cost pricing or other predatory tactics that may be used by the major supermarket chains. In short, any anti-competitive conduct within the retail grocery industry must be vigorously investigated and stamped out.

Where independents can be a competitive third force, consumers will benefit from more choice, better prices and services than those they may receive when faced with a duopoly comprising the two major supermarket chains. Indeed, a competitive third force within the retail grocery industry will protect consumers from the dangers of a cozy duopoly, where price competition is only within a limited range as determined by the duopolists; where there is a lack of real choice as a result of the duopolists refraining from competing on price or service; and where there is a lack of genuine innovation.

2. Key Aspects of NARGA's pro-competitive philosophy

NARGA strongly believes that a competitive third force is critical to the maintenance of vigorous competition within the retail grocery industry. The promotion of competition and the prevention of anti-competitive conduct are an integral part of NARGA's philosophy. The following are central to NARGA's pro-competitive philosophy:

- Ensuring that NARGA members are not placed at a competitive disadvantage by regulatory compliance costs (Compliance costs tend to fall disproportionately on smaller compared with larger businesses). Given the cost sensitive, low profit nature of the retail grocery industry, any compliance costs incurred by independents place them at a cost disadvantage when competing with the major supermarket chains;
- NARGA members expect to buy their supplies at the supplier's best price and if a supplier is selling to a competitor at a cost price lower than the cost price offered to NARGA members, NARGA members are entitled to the same cost price where they make comparable purchases. This is embodied in the principle of 'like terms for like customers' which translates into comparable customers (by reference to volume and services provided) receiving comparable prices;
- Suppliers that discriminate against comparable customers must be identified and any anti-competitive price discrimination appropriately dealt with under the *Trade Practices Act*. Anti-competitive price discrimination arises where independents do not receive comparable prices to those received by the major supermarket chains and, therefore, cannot compete with those chains. Comparable supply prices translate into competitive pricing for consumers. Without comparable prices to those secured by the two major supermarket chains, the independent sector is not as competitive as it could be for the benefit of consumers. Price discrimination between comparable customers can be used strategically to undermine the ability of independents to compete on price. Where price discrimination is demanded by an entity having a substantial degree of market power, suppliers may become party to a tactic employed by the entity to secure for itself an obvious price advantage over rivals;
- Anti-competitive below cost pricing – that is, pricing below cost in selective locations to strategically target an independent competitor - must be identified and appropriately dealt with under the *Trade Practices Act*. Pricing products below cost may give the appearance of being beneficial for consumers, but where below cost pricing is adopted as a strategy by the major supermarket chains to undermine the independent sector, consumers will suffer as prices rise once independents have been eliminated or deterred from engaging in competitive conduct.
- The elimination or undermining of the independent sector is not in the consumer's best interest as independents provide a competitive third force to counter the dominance of the two major supermarket chains. An independent third force provides choice and convenience, and keeps the retail grocery industry competitive for the benefit of consumers. Any predatory conduct by the major supermarket chains aimed selectively at undermining the viability of the independent sector must be stamped out and any further acquisitions of independents by the majors must be closely scrutinized to prevent further increases in the level of market concentration to the detriment of competition in that market.

- A national competition policy that focuses on injecting competitive pressures into highly concentrated industries and ensuring the viability of independents when competing with dominant market players.

NARGA views the above as essential ingredients in the promotion of competition within the retail grocery industry for the ultimate benefit of consumers. A competitive third force will mean competitive grocery prices, greater choice in grocery shopping and the prevention of a cozy duopoly between the two major supermarket chains.

3. Growing Major Chain Dominance and Market Power **- The Problem**

- In 1975 the three major supermarket chains, Coles, Woolworths and Franklins, held **40%**, in 1985 **60%** and in 1998 **80%** of the national grocery market – as reported by AC Nielsen – total defined grocery (refer explanatory note below)¹. With the demise of Franklins, Coles and Woolworths alone will control an **estimated 76 per cent**, a level virtually without precedent in the developed world. **(See attachments 1 and 2).**
- By contrast the top three retail grocers in the UK have **52%**, in Germany **53%**, in France **44%**, in the USA the top five have **34%**, and in Canada **56%**. The level of concentration is quite low in the countries within our region. **(See attachments 3 and 4).**
- The Coles/Bi Lo and Woolworths stranglehold continues to tighten and within twelve months their market dominance could approach and even exceed 80 per cent. The duopoly is anti-competitive and destructive to jobs, small business, and rural and regional communities. As the chains purchase or eliminate their smaller competitors, competition and choice is being reduced and this creates upward pressure on prices to consumers.
- In addition to Coles/Bi Lo and Woolworths opening up to twenty or more new supermarkets every year, the major chains continue to buy out or eliminate their smaller competitors. While the Franklins' break-up has added new stores and returned a number of stores to the independent sector, there is a clear history of the major chains making strategic acquisitions which have the effect of undermining the independent sector.
- There are now vast areas of Australia where the choice for consumers as to where they do their grocery shopping is increasingly coming down to a Woolworths or Coles/Bi Lo supermarket.
- The present competition laws and the ACCC have been unable to effectively deal with the growing tide of unhealthy market domination by the major chains.
- Unless Australia's competition laws are strengthened, Woolworths and Coles/Bi Lo will continue to erode the critical mass needed to support a viable independent sector and a competitive third force in grocery retailing, which is needed to protect consumer interests.

The Solution

The solution lies in the proposed reforms to the Trade Practices Act and National Competition Policy that are set out in Sections 4 and 5 of this Information Pack.

¹ **Note:** The market share figures used in this Information Pack have been sourced from AC Nielsen's ScanTrack service. This service monitors sales through the grocery retailing industry and covers a broad range of packaged grocery categories sold through supermarkets and grocery stores. It includes dairy and frozen foods, but does not cover fresh meat, fruit and vegetables, delicatessen and fresh bakery products, etc. Other categories, such as milk and potato chips, which suppliers deliver direct to store are also excluded, as wholesalers are unable to supply data for these categories.

The figures reported, however, cover more than 100 categories of packaged grocery products and hence are considered a reliable and representative surrogate measure of the market shares held within the supermarket and grocery store sector (i.e., the market for one-stop shopping for food and grocery products).

4 Trade practices reforms – Key NARGA proposals

NARGA is seeking a number of reforms to the *Trade Practices Act* in view of the considerable difficulties currently faced in using s46 (the existing prohibition against misuses of market power) and s50 (the existing prohibition against mergers that substantially lessen competition) to counter specific forms of anti-competitive conduct that may be engaged by the major supermarket chains (namely, Coles and Woolworths). For example, the requirement to prove a predatory intent by the chains is the clearest difficulty faced under the current s46. In particular, the major supermarket chains may engage in conduct that, despite an absence of evidence of a predatory intent, may have a detrimental impact on the level of competition in the market.

In the circumstances, the *Act* should allow this conduct to be assessed objectively to determine whether it has an anti-competitive effect on the market. An 'effects' test in s 46 would permit such an objective assessment. In addition, specific forms of anti-competitive conduct not dealt with under the present *Act* should be prohibited in new provisions of the *Act* to foster effective competition between the major supermarket chains and independent grocery retailers. The *Act* needs to evolve to meet the more sophisticated types of potentially anti-competitive conduct that may be engaged in by the major supermarket chains. This involves fine-tuning existing provisions of the *Act* where appropriate and introducing new prohibitions where existing provisions do not effectively counter specific forms of anti-competitive conduct.

Anti-competitive below cost pricing is one example of conduct that, where engaged in strategically by the major supermarket chains, would undermine competition in a market where independent retailers could not match or sustain prices set by the major supermarket chains. The problem would be magnified in those circumstances where a supplier engages in **anti-competitive price discrimination** whereby the major supermarket chains receive better prices or trading terms than the independent grocery sector for comparable quantities of products. Being sold products at prices higher than those offered to the major supermarket places independent grocery retailers at a clear price disadvantage and prevents the sector from being competitive with the major supermarket chains. Being at a competitive disadvantage forces independent grocery retailers to go out of business or sell out to the supermarket chains. Simply stated, if independent grocery retailers were not at a price disadvantage they could provide effective competition to the major supermarket chains to the benefit of consumers.

A new specific prohibition against **anti-competitive creeping acquisitions** is called for in view of the difficulties faced by the Australian Competition and Consumer Commission (ACCC) under the current s50 in assessing a proposed acquisition by a major supermarket chain by reference to previous small acquisitions by that chain in the particular market. While a large acquisition by the major supermarket chains can, as in the case of the Franklins break-up, be subject to close scrutiny by the ACCC, a series of minor acquisitions that together would substantially lessen competition are less likely to be scrutinised. Where in fact scrutinised, the ACCC faces considerable limitations on its ability to assess the cumulative effect of the creeping acquisitions on the level of competition.

An 'effects' test under s46 of the *Trade Practices Act*

NARGA's concerns with the present s46 stem from the difficulties faced by the ACCC or others relying on the provision in pursuing abuses of market power by the major supermarket chains. In particular, the prohibition against the misuse of market power (s46) has had limited impact in view of the need to demonstrate a particular purpose (as outlined in s46) for the conduct. While 'purpose' can (and often, can only) be demonstrated by inference, the current prohibition does not enable an objective assessment of the conduct's impact on competition in the relevant market (in this case, the retail grocery market) to be undertaken. By amending the current prohibition in s46 to incorporate an **'effects' test** an objective assessment of the conduct on the level of competition can be made to reveal whether or not the conduct of the major supermarket chains operates as a deterrent or hindrance to competitive conduct in the retail grocery sector.

Additional essential reforms

Three specific areas of concern not currently dealt with in an adequate manner by the Act relate to:

- **Anti-competitive creeping acquisitions;**
- **Anti-competitive below cost pricing;**
- **Anti-competitive price discrimination.**

These types of conduct prevent independent retail grocers from competing effectively with the two major supermarket chains. By prohibiting these types of conduct under the *Act*, independent retailers will be able to provide a strong third force in the retail grocery sector. Consumers will benefit from more competitive grocery prices and regional Australia will benefit from a vibrant independent grocery sector.

Anti-competitive creeping acquisitions

Prohibiting **anti-competitive creeping acquisitions** would reduce further anti-competitive concentration of the retail grocery sector. With the major supermarket chains already having a substantial degree of market power and s50's inability to deal with small, yet cumulatively anti-competitive acquisitions, all further acquisitions should be placed under the competitive microscope to assess their impact on competition in the relevant market. Where a proposed new acquisition would, when taken together with previous acquisitions in the market, substantially lessen competition in the market, that acquisition should not be allowed. Given the importance of preventing anti-competitive creeping acquisitions, it is imperative that the ACCC be notified of such proposed acquisitions by the major supermarket chains.

Anti-competitive below cost pricing

Prohibiting **anti-competitive below cost pricing** would ensure that the major supermarket chains would not price grocery items below their acquisition cost as a way of destroying the independent retail grocery sector. Since the major supermarket chains could sustain below cost prices for longer periods of time, it is critical that no below cost

pricing strategy is implemented (unless, for example, it is implemented to match a competitor's price or there is a genuine commercial reason for sustaining losses on a particular product i.e. where it is highly perishable).

Anti-competitive price discrimination

Prohibiting **anti-competitive price discrimination** would prevent suppliers from discriminating between competitors where they buy the same products in comparable quantities having regard to the nature of the buyers and the relationship between the buyers and suppliers. Where similar customers are buying at unexplained price differences, the level of competition in the market is distorted by the fact that one customer has a price advantage over another similarly placed customer. In these circumstances, the price-disadvantaged customer, ie the independent retail grocer, cannot offer the same level of discount to consumers. This acts to the detriment of independent retailers, as they cannot match the prices offered by the major supermarket chains. As independent retailers go out of business or cannot compete and are acquired one by one by the chains, consumers suffer as they are faced with less choice, at prices dictated by major supermarket chains left with no effective competition from independent retailers.

5 National Competition Policy reforms – Key NARGA proposals

NARGA is seeking a number of competition policy reforms aimed at ensuring that the National Competition Council (NCC) places appropriate weight on small business concerns, and social welfare and equity considerations when assessing the public interest. With the NCC placing undue weight on economic efficiency when assessing the public interest, the NCC fails to assess the impact of a particular course of action on the ability of the small business/independent sector of an industry to compete with vertically integrated monopolists, duopolists or oligopolists within that industry. The ability of the small business/independent sector to compete is often a key factor in the promotion of competition.

Similarly, social welfare and equity considerations are often given little or no weight as economic rationalist perspectives are given undue preference in policy advice said to be in the public interest. In the circumstances, the NCC's failure to look beyond economic rationalist perspectives justifies the insertion of a specific power under the *Trade Practices Act* and *Competition Principles Agreement* to enable the Federal, State or Territory Governments to direct the NCC to take into account specific factors in considering whether a course of action is in the public interest.

Importantly, the NCC should, when considering the public interest, also be required to determine alternative courses of action that would reduce concentration within industries. The NCC has not to date focussed on ways to inject competitive pressures into highly concentrated industry sectors such as the retail grocery industry. The NCC should also have a pro-competitive mandate as part of its national competition policy brief. These reforms should be underpinned by appointing a person with small business expertise to the NCC. Alternatively, the Federal, State or Territory Governments may, where faced with a NCC that continues to be unresponsive to the true scope of the public interest, choose to transfer some or all of the NCC's functions to another body.

Strengthen Public Interest Test

Part IIA of the *Trade Practices Act* (the Part of the *Act* governing the operation of the NCC) needs to be amended to expressly require the NCC to consider and specifically report on the possible impact that a particular recommended course of action will have on small business. The preparation of a small business impact study should not only be a requirement for the NCC, but should also be required whenever any legislation review is undertaken at any level of government.

A further amendment is required to specifically include the promotion of small business as a key factor in the application of the public interest test. The present list of factors – as found in clause 1 of the *Competition Principles Agreement* – is limited in scope, particularly as it does not include reference to small business's contribution to competition and the economy. A more expansive definition of the 'public interest' with specific reference to the promotion of small business as a pro-competitive force should be inserted into the *Trade Practices Act* and *Competition Principles Agreement*.

In addition, to ensure that appropriate weight is given to social, equity and small business factors within the National Competition Policy framework, a specific power needs to be inserted into the *Trade Practices Act* and *Competition Principles Agreement* to enable the Federal, State or Territory Governments where appropriate to direct the NCC to expressly take into account such factors when considering whether a course of action is in the public interest.

Pro-competitive mandate

The NCC should be required to inquire into and report on how competition may be promoted in highly concentrated industries. The NCC should not only be required to review legislation that restricts competition, but also to consider mechanisms (whether legislative or non-legislative) to inject competition into those industries in which a small number of players (for example 4 or less) collectively control more than 75% of a market. In considering pro-competitive mechanisms, the NCC is to be specifically required to investigate and report on (revenue-neutral) ways in which the small business/independent sector could be assisted to compete vigorously with those players having a substantial degree of market power.

These pro-competitive investigations could be included in the NCC's work program as allowed for under clause 10 of the *Competition Principles Agreement*.

NCC Small Business Appointment

In keeping with the Federal Government's recognition of the importance of appointing small business representatives to regulatory bodies (see for example appointments made to the ACCC), a small business appointment needs to be made to the NCC. As currently there is no deputy president of the NCC, a small business appointment could be made at this level to demonstrate the importance of the small business/independent sector to the promotion of competition.

Beyond the NCC

Where appropriate weight is given to social, equity and small business factors, and greater emphasis is placed on finding ways to reduce concentration in key industry sectors such as the grocery industry, the NCC will gain support as a truly pro-competitive force. In the absence of such support, the rationale for the NCC's existence will continue to be questioned by regional and rural communities and small business generally. In the face of such questioning, the calls for the modification or abolition will grow louder.

6 GST Compliance Costs - Key NARGA proposals

The Problem

Last year NARGA commissioned national accountancy firm Hall Chadwick to report on the impact of the GST on independent grocers, which are predominantly small family owned and operated businesses.

The April 2001 report found that independent grocery retailers were, on average, spending more than \$1000 a month and almost 19 hours per week just to meet the basic compliance work for the GST (A copy of this report has been provided to all MP's and Senators, as well as key advisers).

According to Hall Chadwick, the on-going cost of compliance – even excluding the cost of preparing the Business Activity Statement – represented 28.25 cents for every GST dollar collected by small business with a turnover up to \$5 million per annum and employing, on average, five full-time staff and a number of part-time employees.

Compare this to the experience of larger businesses with an annual turnover of \$20 million, which the survey found had compliance costs representing 1.25 cents for each of GST dollar collected.

The survey results are stark evidence of the crushing impact the GST has had on the competitive position of small operators, compared with the major supermarket chains, Woolworths and Coles/Bi Lo, which incur relatively low compliance costs.

Most NARGA members are denied the opportunity to gain compliance cost relief due to the unnecessarily restrictive access to Simplified Accounting Methods for Food Retailers, which were established to help smaller food retailers cope with the GST.

On top of this, there are underlying risks to smaller operators due to the complexity with the tax classification of goods, with around 45% of items in a supermarket being taxable and 55% being GST free.

In our view, retailers should not be exposed to liability for uncollected tax/penalties imposed by the Tax Office if they have innocently adopted the tax rate on their supplier's invoice. It is unreasonable to expect small family-owned businesses to become amateur tax experts across the many thousands of goods they sell, and in circumstances where they receive on average some 220 invoices per week.

Also, retail scanning systems within the independent sector can only handle either 10% or tax-free goods, yet are confronted with unnecessary complexity in the way certain goods, including single dose painkillers and mixed supplies, are treated.

The Solution – Making the GST Simpler and Fairer for Small Business

In the interests of a simpler and fairer GST, NARGA is calling for:

- Major and sensible reform of the Simplified Accounting Methods for Food Retailers to ensure that they provide the relief intended for independent grocery retailers who have been hit hardest by GST compliance costs (a consultative process has commenced with the ATO to address our concerns).
- Innocent errors (i.e., relying on a supplier's tax invoice for tax classification of goods) to be accepted as a defence against action by the ATO to recover unpaid and uncollected taxes.
- the removal of unnecessary complexity/anomalies re the tax classification of goods, e.g., tax treatment of single dose pain killers (e.g., Paracetamol) and mixed supplies (e.g., hampers).

Retail Grocery Market Shares

AC Nielsen total defined grocery – (Source: ScanTrack)

Woolworths/Coles Bi Lo

1999-2001

The Growing Market Stranglehold of Woolworths and Coles Bi Lo

State	Woolworths			Coles/Bi Lo			Combined Total			NARGA Est * 2002
	1999	2000	2001	1999	2000	2001	1999	2000	2001	
NSW/ACT	36.3	38.2	40.6	26.1	28.2	30.3	62.4	66.4	70.9	
Vic	36.9	37.7	38.4	35.0	36.4	37.1	71.9	74.1	75.5	
Qld	38.8	39.9	40.6	33.2	33.1	34.2	72.0	73.0	75.2	
SA	30.0	30.8	31.1	39.9	40.8	41.9	69.9	71.6	73.0	
WA	26.6	27.1	28.2	34.3	34.6	34.5	60.9	61.7	62.7	
Tas	57.3	56.9	57.3	29.0	28.1	29.4	86.3	85.0	86.7	
National	35.9	37.1	38.3	31.9	33.1	34.3	67.8	70.2	72.6	76.0

Source: Retail World December 2001 using AC Nielsen figures for total defined grocery. MAT's to 31 October 1999, 29 October 2000 and 28 October 2001. (Source: ScanTrack)

* Includes the additional stores acquired from the break-up of Franklins, which will increase the national market share of the major chain duopoly to around 76% (NARGA estimate)