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A SUBMISSION TO

THE DAWSON COMMITTEE
REVIEW OF THE TRADE PRACTICES ACT

'RESTORING COMPETITIVE EQUALITY IN AN INCREASINGLY ANTI-COMPETITIVE ENVIRONMENT'

Prepared by

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PREAMBLE

The Western Australian Independent Grocers Association ("WAIGA") commends the Federal Government's initiative to conduct this Review into the Trade Practices Act.

In the space of just 25 years, the notion of genuine competition in the Australian grocery and supermarket industry has evaporated to the point where we, as independent retailers, now consider the development horizons for our business in three to five year time spans.

Highlighting this disturbing position is the fact that in just 25 years the competitive balance in the Australian grocery industry has shifted from a position where in 1975, independent grocers accounted for around 80 percent of sales to 2000, where the sector is responsible for a paltry 23 percent of the market.

Indeed, it is worth noting that had it not been for the intervention of the Australian Competition and Consumer Commission in the sale of the Franklins Group in 2000/01, this market share would most likely have fallen well below the 20 percent level.

The Dawson Committee Review of the Trade Practices Act therefore represents a watershed opportunity to contain or possibly reverse the erosion of grocery sector competitiveness in Australia. We believe that unless substantive action is taken in respect of the matters highlighted in this submission, competition and the benefits that should accrue to consumers will steadily decline.

We are aware that the National Association of Independent Grocers ("NARGA") is also preparing a submission to the Committee. Our Association unreservedly endorses and supports NARGA's recommendations, which span a considerable breadth of issues confronting the future of Australia's grocery industry.

WAIGA - A BRIEF BACKGROUND

The W.A. Independent Grocers' Association Inc. was established in 1990 to represent the interests of its members in dealings with suppliers and government. The Association is an active member of the National Association of Retail Grocers Inc (NARGA) and through that membership, the Council of Small Business Organisations of Australia (COSBOA).

The Association's principal constituency is comprised of about 700 privately owned metropolitan and regional grocery stores operating under the following banner names:

- Dewsons
- Foodland
- Farmer Jacks
- Supa Valu
- Four Square

Additional to these are numerous non-franchised, full-service supermarkets, individual grocery stores and mini-mart delicatessens, which carry limited grocery lines in conjunction with confectioneries, soft drinks and consumer convenience products.

In total, WAIGA's members employ more than 15,000 Western Australians, account for around $1.2 billion in sales, or about 26 percent of the WA grocery market, and almost 100 million customer transactions per year.

COMPETITIVE EQUALITY - A SUMMARY OF THE ISSUES

The following outline of issues and fundamental market inequities has been prepared based on the collective experience of WAIGA's membership.

Although supporting the aims and objectives of the Trade Practices Act, this Association is now of the belief that the Act's effectiveness has been overtaken by the strategies and tactics employed by major grocery industry players in this country. Accordingly, this review presents a genuine opportunity for the restoration of confidence in the ability of Government to administer equity and balance for both commerce and consumers.

At the heart of our concerns is the accelerating dominance enjoyed and employed by key players in Australia's grocery sector. This aggressive accumulation of market share by the Coles and Woolworths supermarket duopoly in particular, now accounts for almost 80 percent of grocery sales in Australia. This is a situation almost unique in western nations. As such, these levels of market power in a country the size of Australia demand the imposition of more stringent and effective levels of regulation.

Accordingly, we draw the Committee's attention to actions which both individually and in combination serve to undermine the goal of genuine competition in the marketplace.

Excessive Market Power

First among these is the misuse of market power to undermine the ability of small grocery industry competitors to purchase goods at the same wholesale prices achieved by the large supermarket chains. In numerous instances the chains have been able to retail products at prices far below the cost to independent grocers, even though the independents, through their own group buying arrangements, purchased the same quantities of the identical product.

Anti-Competitive Pricing

Secondly, we highlight the regularly excessive and wilful use of extended price discounting as a tactic to undermine the market share of smaller independent grocery industry retailers. Price-leading is a common and accepted tactic used by virtually all retailers, however, its principal weakness, is that prolonged use has a significant affect on already slim profit margins. For retailers with the deep financial resources of Coles and Woolworths, price-leading targeted at competing stores for periods exceeding the weekly-advertised cycle is a regular occurrence which independent competitors have little ability to withstand.

Cheque Book Dominance

Thirdly, we point to the strategy of cheque-book acquisition in which strategically located individual and small groups of successful independent supermarkets are purchased quietly and gradually by both major chains. This practice, which has accelerated over the last decade, has delivered market share to the tune of billions of dollars to Coles and Woolworths. Not surprisingly, both companies are now applying this tactic with considerable success in the liquor industry.

Centralised Buying

Lastly and as a consequence of their need for corporate efficiencies and increased profitability, is the use of national, centralised buying and distribution systems. These systemised operations deprive hundreds of small and medium size manufacturers, rural producers and growers of the opportunity to develop and expand their enterprises, which in turn, would act to underwrite far higher levels of competition within the market.

Examples of this practice in Perth include the chains' long-standing policy of bypassing the local wholesale fruit and vegetable markets in favour of direct supply contracts or the bulk transporting of produce from the eastern states. The company also employs a similar practice in respect of red meat supplies resulting in the loss of sales and employment for WA livestock producers and abattoirs.

The bypassing of local suppliers also impacts on the competitiveness of independent rural and regional grocers and retailers, and ultimately consumers. In this respect, the cost and inconvenience of servicing and supplying retailers with low volumes of perishable produce becomes prohibitive, eventually leading to a reduction in the range of goods carried by the store. For consumers, the only option is to purchase these lines from supermarkets owned by the major chains, which in most instances, are located in major regional centres.

When these issues are viewed in aggregate, it is little wonder that over the last quarter century, the balance of market share in the Australian grocery industry has been inverted, from a position of genuine competitiveness where independent grocers accounted for around 80 percent of sales in 1975. Today, the sector is responsible for a paltry 23 percent of the market.

It is worth noting that if not for the intervention of the Australian Competition and Consumer Commission in the sale of the failed Franklins Group in 2000/01, this market share would most likely have fallen well below 20 percent level.

ISSUES BACKGROUND

Pricing

Virtually all independent grocers are confronted with the use of three types of aggressive pricing strategies. These interlinked strategies have been developed and refined by the major supermarket duopoly over the years as a result of their massive financial resources and purchasing power.

In brief, these strategies comprise:

- The ability to achieve wholesale prices significantly below those available to independent retailers, where both the major supermarkets and independent grocers are purchasing similar quantities of the same product
- The extended use of unreasonably low retail pricing of goods

The use of these strategies, either singularly or in combination, presents independent grocers with a virtually insurmountable barrier to providing genuine competition and hence, benefits for consumers.

Additional to the direct impact of this strategy on independent retailers, is also the effect on overall market competitiveness. In this respect, reduced sales result in lower re-order rates, which when viewed in the context of several hundred stores, results in reduced warehouse efficiencies. These reduced efficiencies then proceed to reduce the group's ability to secure competitive prices from manufacturers and wholesalers.

In Western Australia, the chains are able to negotiate directly with farms and farming districts for the purchase of entire outputs of produce and livestock. This not only achieves massively reduced farm-gate prices, but also effectively eliminates agents, wholesalers and wholesale marketing systems such as the Canning Vale markets. Reductions in cost prices are then either retained as extra profits, or used to undercut local independents that use the market system.

Extended price discounting or "price leading" is a regular occurrence across a range of goods. This practice affects both independent grocers and smaller convenience retailers, the latter relying on emergency top-up and incidental sales to maintain, not just their competitiveness, but in many instances their survival.

The tactic involves selling high volume lines not on a weekly basis, as is common in the industry, but for weeks on end, at below cost or near-cost, with the aim of drawing customers away from nearby independent stores and thereby robbing these establishments of sales and profit.

Recommendations:

Regulatory initiatives be introduced to:

- Ensure that retailers receive equal treatment in respect of transactions involving "like-for-like" purchases
- Outlaw sales of products at prices significantly below regular margins for extended periods

Growth through Acquisition and Merger

Over the last decade, a significant proportion of this market share has been achieved through the acquisition of independent supermarkets and small privately owned chains.

As the chart over page indicates, 28 grocery stores with annual sales of $305.7 million have been acquired by the major chains (Coles/Woolworths) between 1996 and 2000 in metropolitan and regional Western Australia.

These transfers of ownership have not only stymied competition, but have also transferred a significant proportion of previously local manufacturing activity out of WA as a result of the major chains' policy of centralised buying programs. Additionally, but less obviously, they have also reduced the warehouse operating efficiencies of the WA-based grocery wholesaler, FAL.

Acquisition of Independent WA Grocery Stores 1996 – 2000

STORE NAME	ANNUAL WAREHOUSE PURCHASES $M	ANNUAL STORE SALES $M	PURCHASER
Supa Valu Kalgoorlie	2.80	7.00	Coles
Supa Valu Mundaring	6.80	17.00	Coles
Newmart (6 stores)	29.90	93.55	Coles
Farmer Jacks Beechboro	8.30	20.80	Coles
Charlie Carters (15 stores)	30.25	75.65	Coles
Advantage (4 stores)	33.10	91.70	Woolworths
TOTAL	**$111.15M**	**$305.7M**	

Although it is recognised that the sale of businesses is a normal and natural characteristic within a competitive market, serious questions have arisen in regard to the prices paid for a number of independently owned grocery stores by the major chains. Indeed, WAIGA is aware that the purchase of Advantage grocery stores by Woolworths was substantially above current market values for similar businesses, which naturally resulted in the failure of competitive bids. In such instances it is understandable that independent grocery store owners felt almost compelled to accept the offer for their business.

Currently the level of scrutiny is far higher in instances where a chain proposes to purchase another chain's stores, than where the same chain purchases an independent outlet.

This growth strategy has been repeated elsewhere in Australia with the acquisition of 107 independent grocery stores between 1995 and 2000. Total annual retail sales from these stores amounted to almost $1.35 billion with annual wholesale purchases in excess of half a billion dollars.

Recommendations:

Introduce regulations requiring:

- Justification of any further acquisitions where four or less market participants control more than 75 percent of the market
- In the event that the 75 percent rule is breached, the acquirer be required to divest assets or operations to ensure that the aggregate of ownership does not exceed 75 percent
- Formal assessment in regard to the impact on small business, consumers and the general level of competition in advance of any settlement where the level of aggregate market share will not exceed the 75 percent limit.