NARGA

National Association of Retail Grocers of Australia Pty Ltd ABN 72 000 446 355

Tel: 61 2) 9585 0721
Fax: 61 2) 9579 2746
Email: info@narga.com.au

Suite 9, Level 2, 33 MacMahon Street
Hurstville NSW 2220
www.narga.com.au

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The General Manager
Competition and Consumer Policy Division
The Treasury
Langton Crescent
PARKES ACT 2600

Email: creepingacquisitions@treasury.gov.au

Dear Sir or Madam,

Creeping Acquisitions – The Way Forward

NARGA represents the independent retail grocery sector comprising over 5000 stores employing more than 225,000 people.

The independent grocery sector now comprises less than 20% of the national grocery market, yet provides essential supplies to thousands of regional and remote communities, particularly those considered too small to be of interest to the major supermarket chains, as well as providing competitive pressure to those chains through larger stores in metropolitan and regional centres.

The ongoing viability of the independent network is dependent on their share of the market not shrinking to the stage where that wholesaling and distribution network becomes unviable.

The level of concentration in the national grocery market is highlighted by the following examples taken from the ACCC report on their recent inquiry into the sector.

The report says that chains have 87% of stores over 2000 sq metres in size and 96% of stores over 3000 sq metres in size (which have the highest turnover). The ACCC also suggests that the sector has a high HHI[1] - even with the ACCC's reduced (70%) estimate of the majors' combined market share:

[1] The **Herfindahl index**, also known as **Herfindahl-Hirschman Index** or **HHI**, is a measure of the size of firms in relationship to the industry and an indicator of the amount of competition among them. Named after economists Orris C. Herfindahl and Albert O. Hirschman, it is an economic concept but widely applied in competition law and antitrust. It is defined as the sum of the squares of the market shares of each individual firm: ie the average market share, weighted by market share. As such, it can range from 0 to 10,000 moving from a very large amount of very small firms to a single monopolistic producer. 1 1 1 1 (cont.) Decreases in

The ACCC report said[2]:

> The HHI for the retailing of packaged groceries based on this assessment of sales shares is between 2750 and 3000. Although these figures show a high level of concentration in this segment of the retail grocery industry, other factors including barriers to entry and expansion must be considered before any conclusions are drawn on the effectiveness of competition.

The question that now must be asked is whether further concentration in the sector is desirable and, if not, what can be done to address the issue?

Preventing further concentration in the sector

In the current discussion paper, the Treasury has proposed two regulatory models aimed at addressing the 'creeping acquisition' issue. Both are based on the 'substantial market power' (SMP) model. The amended version of SMP reads as follows:

> (1) *A corporation that has a substantial degree of power in a market must not directly or indirectly:*
>
> *(a) Acquire shares in the capital of a body corporate; or*
>
> *(b) Acquire any assets of a person;*
>
> *If the acquisition would have the effect, or be likely to have the effect, of enhancing that corporation's substantial market power in that market.*

Using this approach there would need to be an accepted definition of 'enhance' that relates quite clearly to any increase in market power, through increase in market share in the affected market or through an increase in the measured HHI.

We understand that the new requirements would operate in addition to the existing mergers and acquisition tests in Section 50 of the Act, and that the requirement to consider the 'market' as a '*market....in (a) Australia; or (b) a State; or (c)a Territory; or (d) a region of Australia'* also applies.

Our only comment in relation to the latter is to suggest that it should be made clear that, when assessing an acquisition, the regulator should be looking at the potential impact on each and every one of these markets in order to fully test the potential effect. That is, as a 'market' ....in (a) Australia; *and* (b) a State; *and* (c) a Territory; *and* (d) a region of Australia.

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the Herfindahl index generally indicate a loss of market power and an increase in competition, whereas increases imply the opposite.

[2] *Report of the ACCC inquiry into the competitiveness of retail prices for standard groceries,* Australian Competition and Consumer Commission, July 2008, p. 51

In the case of competition in local markets we suggest that the use of HHI as a measure of concentration could be augmented by a measure suggested during the UK Competition Commission inquiry into their grocery industry, where it was suggested that an entity's share of the local market could be related to the relative size of its retail space in relation to the total retail space taken up by that sector in the area. (Note that here a clear distinction was made by the UK commission between supermarkets as opposed to non supermarket grocery outlets – e.g. convenience stores and other food retailers.)

The UK CC suggestion is that should a particular retailer have a share of that retail space of 60% or larger that they would only be allowed to occupy additional space in that locality if they were to divest themselves of sufficient space so as to reduce their share to 60% or less. Such a reduction would occur only if the freed retail space was made available to a competitor, i.e. not simply transferred to another entity within the conglomerate where, as an example, a space vacated by a Woolworths or Wesfarmers related entity is simply transferred to another such entity within the group (say a Dan Murphy's liquor store or a K-Mart) and thereby denied to a competitor.

The ACCC has made it clear that the current form of s50 already gives it the power to act in this way.

Guidelines could be issued in relation to the acquisition of other businesses, leases or development sites that make it clear what the limits are in terms of regional market share expressed in terms of the HHI and /or in terms of share of retail space.

The current discussion paper suggests that another option would be for the Act to provide for the responsible minister to declare a corporation or a product or service sector as being source of harm to competition if it were to be allowed to make further acquisitions of existing businesses. Such a declaration would trigger a requirement for entities in the affected sector or the corporation to be compelled to notify the ACCC of further acquisitions.

Given the lack of compliance with notification requirements under the current voluntary code, we would support a system of declaration and compulsory notification.

It is further suggested that the minister could set thresholds for such mandatory notification of acquisitions. However, we would contend that the grocery retail sector is already so concentrated that *any* acquisition by the major chains has the potential of further harm to competition in the sector. Therefore they should be required to notify the ACCC of any proposed acquisition by them and such an acquisition should be subjected to the ACCC merger assessment process.

We support the declaration concept and suggest that Woolworths and Wesfarmers should be the first two entities subject to such a declaration.

Summary and recommendation

We recommend that:

- the amendment to Section 50 of the Act outlined in the Discussion Paper be made to the Act.
- the Act be amended to require the prior notification of acquisitions, including acquisitions of sites and new leases, by dominant corporations in a market that is concentrated as determined by ministerial declaration.
- that, at the local level, the HHI be used as a measure of market concentration in the retail grocery sector, possibly supplemented by guidelines relating to other measures of relative market share.

Please contact us should you require further details.

Yours sincerely

Ken Henrick
Chief Executive Officer