



**Woolworths New Zealand Limited's submission on the New Zealand
Commerce Commission's draft report regarding the market study
into the retail grocery sector**

10 September 2021

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Summary of Woolworths New Zealand's submission

1. Introduction

- 1.1. Woolworths New Zealand Limited (**WWNZ**) has been part of New Zealand communities for more than 90 years, through our Countdown, SuperValue and FreshChoice supermarkets, and our Foodtown, Woolworths and Big Fresh stores before that. Our purpose across the business is to make Kiwis' lives a little better every day. We have an unwavering commitment to contribute positively to Aotearoa, and our team of more than 20,000 people work hard to deliver safe, fresh, and affordable groceries to New Zealanders - making us one of the largest employers in New Zealand. We have also continued to increase our commitment to, and investment in, community, charity and sustainability initiatives, including our 2025 Sustainability Plan *Kia pai ake te āpōpō - A Better Tomorrow*. We know we have a privileged position in our community, and that is not something we take lightly.
- 1.2. This is why we have welcomed the Commerce Commission's (**Commission**) market study into the retail grocery sector (**Market Study**) from the outset, and we have engaged positively and collaboratively with the Commission throughout. We welcome the opportunity to provide this submission (**Submission**) on the Commission's draft report (**Draft Report**). Our Submission begins with a summary of our views on the Draft Report (pages 3 to 27), before Parts A to D (pages 28 to 116) provide more details.
- 1.3. We acknowledge that the Commission has, in its Draft Report, identified areas where it considers the sector can improve. We are committed to working constructively with the Commission and the Government to help address these areas in a way that will make positive changes for the benefit of Kiwis. While we consider that our market is already intensely competitive, we are open to a number of the measures proposed by the Commission. We share the goal of making groceries more affordable and delivering positive outcomes for New Zealanders.
- 1.4. We do not, however, agree with all of the preliminary findings in the Draft Report. Some of the analysis in the Draft Report does not accurately reflect the level of returns, the dynamics of grocery prices, nor the nature of competition in the retail grocery sector in New Zealand. For example, the Draft Report:
 - 1.4.1. Does not mention that grocery food prices have actually fallen in real terms over the last decade (something we think should have been a key feature).
 - 1.4.2. Significantly overstates our returns (when the reality is we are a low margin business).
 - 1.4.3. Significantly overstates how New Zealand retail grocery prices compare to other countries (when the evidence shows our prices are competitive).
 - 1.4.4. Does not address the many factors that impact retail grocery prices (such as GST, supplier returns, export commodity prices, and the costs to serve a small isolated market such as New Zealand).
 - 1.4.5. Significantly understates the high levels of change and innovation in the sector, including trends towards convenience and online grocery shopping.

- 1.5. We know that the price of food and other groceries matters deeply to all New Zealanders, and so getting this Market Study right is extremely important.
- 1.6. In this summary, we outline our views on some of the Commission's preliminary findings, before commenting on the options we support and believe could result in positive change for the benefit of Kiwis - including options that have been "tried and tested" overseas. This includes the introduction of a Grocery Code and a Unit Pricing Code; appointment of a grocery ombudsman or adjudicator; simplification of pricing, promotions, and loyalty programme terms; and waiver of "no supermarket" provisions in leases and land covenants. Such measures have worked well for consumers, suppliers, and the industry in Australia and elsewhere. We also support changes to New Zealand's planning regulations, Resource Management Act 1991 (**RMA**), and Overseas Investment Act 2005 (**OIA**) to assist in entry and development of new retail grocery sites.
- 1.7. Some of the other more significant and novel options put forward by the Commission however carry a very high risk of adverse consequences to the efficiency, prices and service levels that could be offered to Kiwi consumers. Unprecedented regulatory intervention as has been suggested in the Draft Report should be positioned as a last resort, and should not be seriously proposed or adopted until other "tried and tested" measures have been implemented, given time, and their impact and effectiveness have been reviewed.
- 1.8. We think it is important that the Commission update its preliminary findings to reflect the issues we have identified with the Draft Report, and that the Commission focus on options that are less risky and more likely to result in overall benefits for New Zealand consumers.

2. Our view on the Commission's key preliminary findings

2.1. Grocery prices in New Zealand do not suggest that there is an issue with competition

- 2.1.1. We understand why there is such interest in New Zealand's grocery prices, and how they compare to other countries. However, making accurate comparisons is not easy. In our view, the way the Commission has analysed this issue in the Draft Report means the comparisons the Commission has made are not accurate, and the preliminary findings about competition are not supported.

2.1.2. Grocery food prices have actually fallen in real terms

- 2.1.2.1. The Draft Report states that "a firm in a workably competitive market will find it hard to raise prices",¹ and that in markets where "competition is less intense" grocery retailers would have an incentive to increase prices.² We agree, which is why the fact that retail grocery food prices have decreased in real terms (that is, grown more slowly than the consumer price index (**CPI**)³ and input costs) over the last decade should have been a key feature of the Draft Report.

- 2.1.2.2. We have worked hard over the last decade to restrict our own retail price inflation to 0.7% per annum at Countdown (well below CPI of 1.6% per annum and increases in input costs of 1.7% to 3.7% per annum). If competition was not working in the sector, then increased input costs

¹ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [5.28].

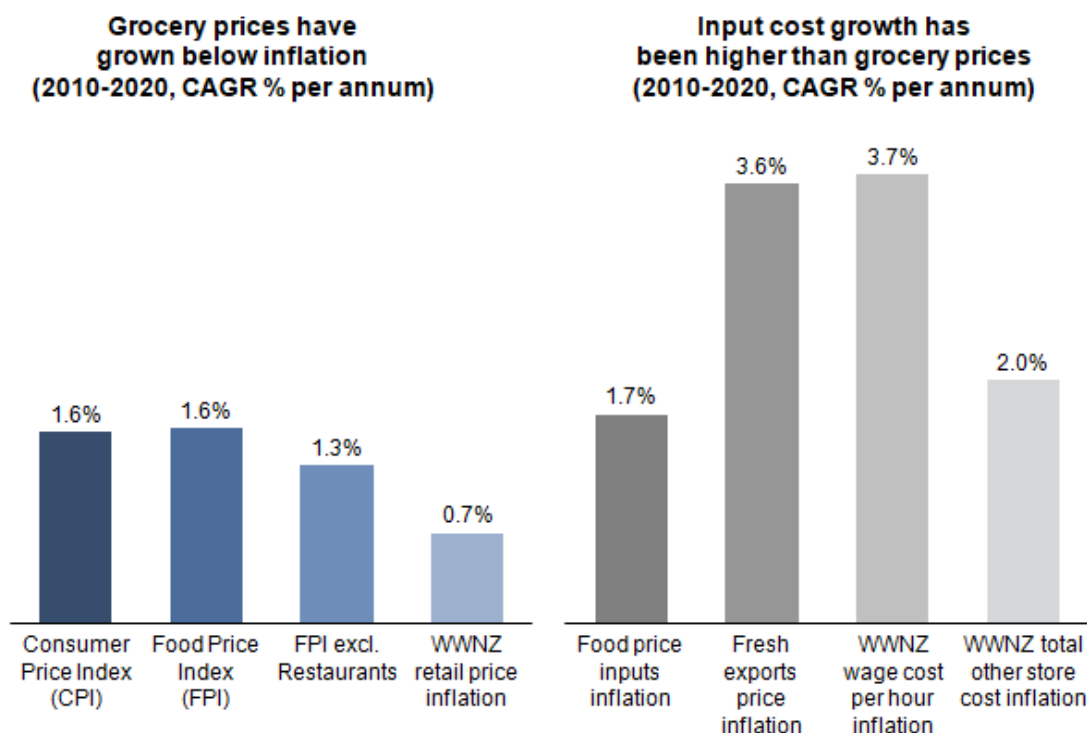
² Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [4.51].

³ Consumer Price Index.

would have been not only passed through to consumers, but more than passed through. This has not happened. Instead, competition has fueled efficiency - reduced stock loss and wastage, improved supply chain innovation and productivity, and improved in-store processes - all of which have controlled costs while delivering competitive prices.

2.1.2.3. The fact that retail grocery food prices have fallen in real terms over the past decade is something that we think Kiwis should know.

Exhibit 1: New Zealand retail grocery prices, input costs, and export prices



2.1.3. There are issues with the Draft Report's international price comparisons which mean they should be re-stated to improve accuracy

2.1.3.1. There are difficulties in making international comparisons about food prices and these have been understated by the Commission: There are many factors that impact the prices that consumers pay for groceries (as outlined in our Initial Submission and further in paragraphs 26.2 to 26.3 in Part D).⁴ This makes it very difficult to make accurate comparisons of retail prices between countries. Other competition regulators have recognised this.⁵ Despite this, the Commission has placed great weight on its comparisons, in particular by suggesting that New Zealand prices

⁴ See WWNZ's "Submission on the Commerce Commission's Preliminary Issues Paper" (4 February 2021). These include differences in taxes (including GST), product quality, global and local supply chains, input costs, regulatory settings (for example, import biosecurity requirements and agricultural subsidies, among many other factors).

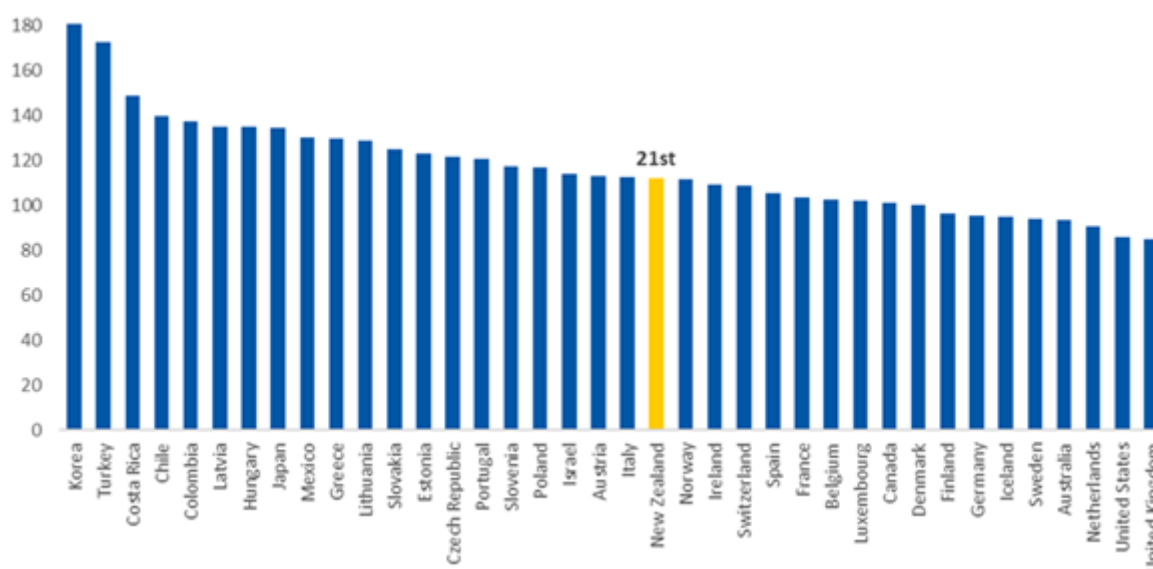
⁵ As the UK Competition Commission (**UKCC**) observed in its 2007 Grocery Market Study: "International comparisons of prices are difficult to make as a result of exchange rate issues, comparability of products and pack sizes, the role of tax in food prices, and different property markets and planning regimes. For these reasons, we consider that the value of any extensive cross-country comparison would be limited."

rank sixth⁶ among the 38 countries of the OECD.

2.1.3.2. There are issues with the Commission's price comparison methodology:

These include choosing not to use a Price Purchase Parity (**PPP**) approach to comparing to other countries (which would drop New Zealand to twenty-first in the OECD), nor sensitivity testing using PPP (both of which would ordinarily be done by the Commission when comparing prices to other countries);⁷ dismissing EIU data presented by NERA Economic Consulting (**NERA**) that indicated that retail grocery prices in New Zealand are not high compared to other OECD countries; and stating that “New Zealanders appear to spend a relatively high proportion of their income on groceries”⁸ when the Draft Report did not, in fact, include any analysis of grocery expenditure compared to income to support that statement. When grocery expenditure is looked at as a proportion of gross national income, New Zealand's expenditure ranks seventeenth. See Exhibits 2 and 3 below, and paragraph 26.4 in Part D.

Exhibit 2: Grocery price level indices excluding alcohol and tobacco using PPP rates (2017)⁹



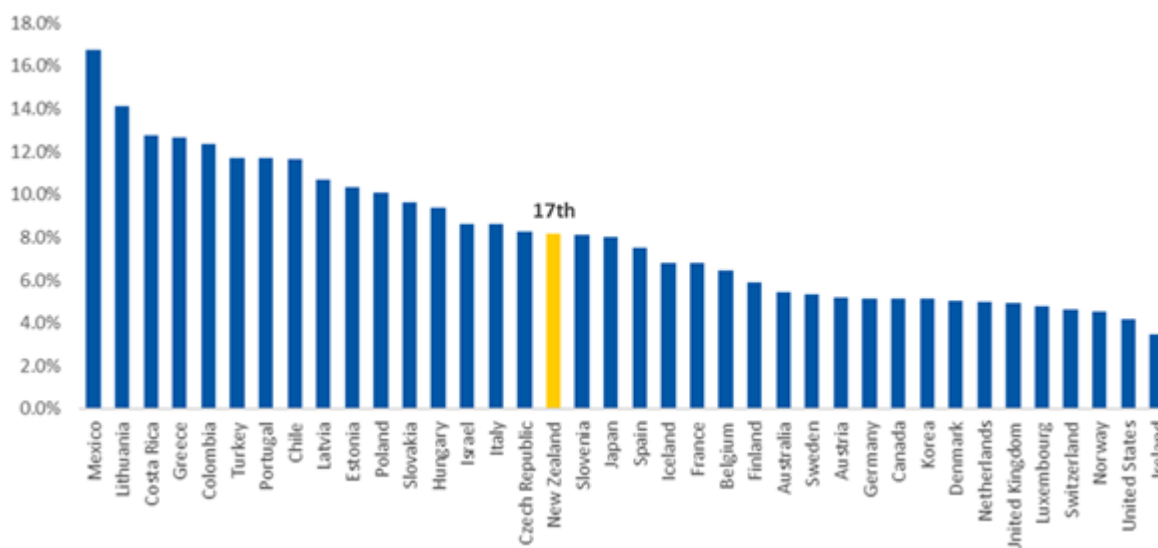
⁶ Even adopting the Commission's own analysis, we do not consider that this reference to “sixth” ranking is an accurate way to portray the outcomes of that analysis, because the Draft Report then goes on to state that New Zealand ranked between sixth and eleventh out of the 38 countries of the OECD (depending on the dataset used).

⁷ As it did in its Mobile Market Study, amongst other benchmarking analyses. The Commission's reason for not using PPP in this case is also inconsistent with Statistics New Zealand's definition of the “supermarket and grocery stores” industry as “non-tradable”. See: https://comcom.govt.nz/__data/assets/pdf_file/0022/177331/Mobile-Market-Study-Findings-report-26-September-2019.PDF

⁸ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [3.20].

⁹ This price level index measures whether the price level for groceries is higher or lower relative to the general price level in the country. Source: OECD.Stat, 2017 PPP Benchmark results, Table 1.11: Price level indices (OECD=100).

Exhibit 3: Expenditure on groceries per capita as a percent of GNI per capita using market exchange rates (2017)¹⁰



2.1.4. There are clearly many other factors beyond competition at play

2.1.4.1. The New Zealand market realities mean there are high costs across the economy, and so New Zealand is an expensive place overall: The same OECD dataset and approach used by the Commission suggests that New Zealand has a comparatively high price ranking across **all** sectors of the economy (eighth overall), not just groceries. See Exhibit 4 below. These reflect the realities of serving a small remote market that is spread across a long, skinny island chain. This is relevant to assessing how New Zealand's grocery prices compare to other countries, and whether differences in competition are a material factor in those comparisons. The Draft Report does not acknowledge that. Clearly other dynamics, which apply across the whole of the economy, are at play (for example, scale, distance, tax, and other costs of doing business in New Zealand).

2.1.4.2. Different input costs can be a significant factor: For example, analysis by Woolworths Group on the subset of ~7,500 identical (barcode matched) longlife grocery and general merchandise products that are stocked in both WWNZ and Woolworths Australia shows that WWNZ has to pay approximately 10% more on average for these same products than Woolworths Australia (these figures exclude GST). Despite this, WWNZ on average sells these products at a similar retail price (again, excluding

¹⁰ Source: World Bank, ICP 2017 results and World Bank DataBank, World Development Indicators.

GST).¹¹

- 2.1.4.3. If our business made no profit, this would still not change New Zealand's food price ranking in the eyes of the Commission: We are highly focused on controlling costs to help deliver competitive prices, including reduced stock loss, improved supply chain productivity, and improved in-store processes. Our margins are 2.4c for every \$1 spent in our stores.¹² Even if we made no profit at all, New Zealand's price ranking (based on the Commission's view) would still not change relative to other OECD countries.¹³ Other commentators have noted this also.¹⁴
- 2.1.4.4. Multinational supplier margins have a greater impact than retailer margins: For every \$1 spent by a customer in a Countdown supermarket, we pay 63 cents directly to our suppliers, and the evidence is that suppliers' profits have a greater impact on the prices of groceries in New Zealand than grocery retailers' margins. Demonstrating this, in many categories a small number of multinational suppliers account for 60% to 90% of products sold (for example, Unilever, Coca-Cola Amatil, Nestle, Procter & Gamble, Pepsico, Mondelez and others),¹⁵ and those suppliers typically have EBIT margins in the range of 10% to 30% (compared to WWNZ with around 5%) and a pre-tax Return on Capital Employed¹⁶ of 10% to 20%¹⁷ (compared to WWNZ with a pre-tax Return on Capital Employed around 8% to 9%).¹⁸ See Exhibit 5 below.
- 2.1.4.5. GST has not been factored in: New Zealand takes a different approach to many other countries in taxing groceries at the same rate (15%) as other goods and services.¹⁹ Australia exempts fruit and vegetables, meat, and most basic foods from their GST rate of 10% and the UK exempts most food from VAT. GST makes a far larger difference to the prices of groceries in New Zealand than supermarket profits. The Draft Report expressly said that "the impact of GST on grocery prices" has not been

¹¹ This comparison has been performed by adjusting for exchange rate differences (using the average exchange rate for the period). These common barcode matched products represent a subset of longlife products equivalent to approximately [] of Countdown's total sales value. Woolworths Australia ultimately has very similar EBIT margin outcomes as WWNZ as a result of higher costs in some other areas (and to a lesser extent other mix dynamics), and operates in a grocery market with Coles, Aldi, Metcash/IGA, Costco and now Amazon that is acknowledged as being "highly competitive" (for example, Bankwest Future of Business: Focus on Supermarkets Report (2019): Available at: <https://www.bankwest.com.au/content/dam/bankwest/documents/business/insights/focus-on-supermarkets-report-2019.pdf>)

¹² FY2020.

¹³ Analysis by WWNZ and NERA.

¹⁴ (15 August 2021). Commerce Commission's supermarket report reveals lack of competition is 'trivial'. Stuff Available at:

<https://www.stuff.co.nz/national/politics/opinion/300381939/commerce-commissions-supermarket-report-reveals-lack-of-competition-is-trivial>

¹⁵ [] of our sales come from products sold to us by just []% of our suppliers.

¹⁶ Note: Return on Capital Employed (ROCE) is a pre tax measure of return.

¹⁷ Or a pre-tax Return on Capital Employed as high as 24%-37% in the case of some multinational suppliers that separately report results in New Zealand.

¹⁸ These Return on Capital Employed figures are pre-tax, and calculated using a different methodology to that used in the Draft Report. See footnote 22 for more information.

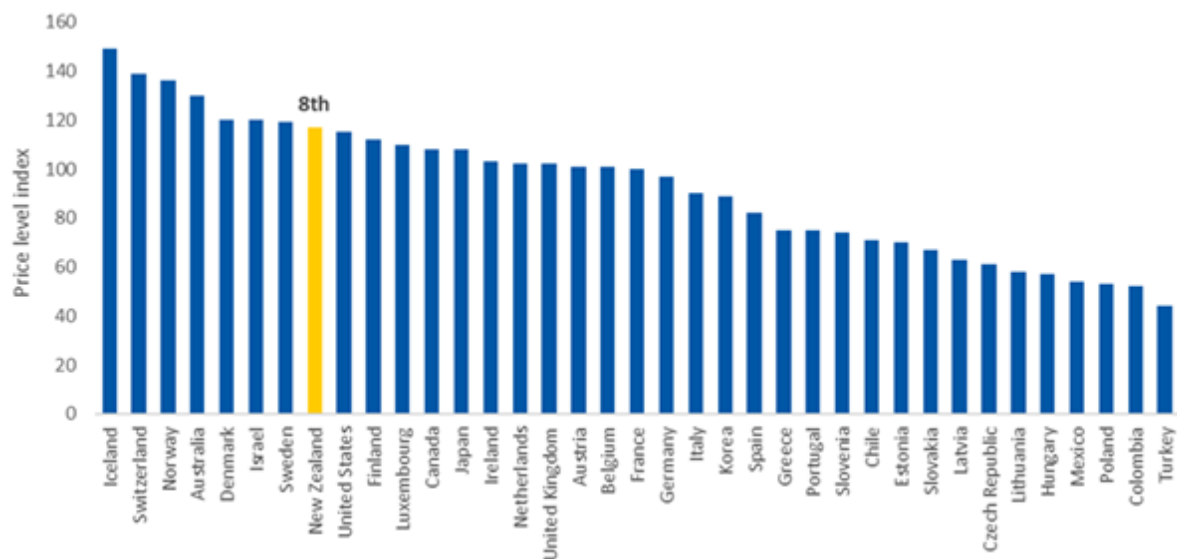
¹⁹ (28 April 2008) Removal of GST on food unlikely - PM. NZ Herald. Retrieved from:

<https://www.nzherald.co.nz/nz/removal-of-gst-on-food-unlikely-pm/GUQOBX2ONXIL7EYLG7DHQTUEKA/>

considered. That is a significant exclusion.²⁰

- 2.1.4.6. Export commodity prices have not been factored in: In New Zealand, export markets are by far the biggest market for many of our farmers and growers. This means that export prices for key New Zealand grocery exports (dairy, meat, fish, and fruits and vegetables), have a significant impact on food prices in New Zealand. The Draft Report did not address this.

Exhibit 4: Comparing price levels across all sectors in the economy combined using the Commission's approach to comparisons (2017)²¹

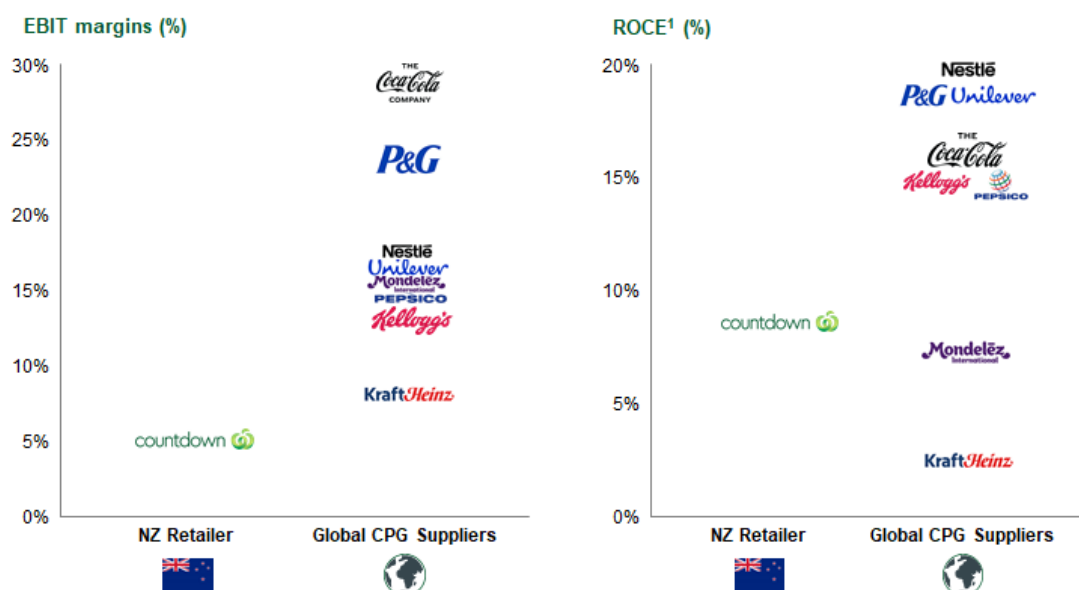


²⁰ The Draft Report (at [1.10]) states that “the impact of GST on grocery prices” has not been considered. That is a significant exclusion given the Draft Report is attempting to compare retail prices between countries.

²¹ Source: OECD.Stat, 2017 PPP Benchmark results, Table 1.11: Price level indices (OECD=100). This chart shows price level comparisons between countries across all sectors adopting the same approach that the Commission adopted in the Draft Report to showing price level comparisons between countries for grocery prices. As noted elsewhere in this Submission, WWNZ considers there are issues with the Commission's approach to comparing price levels between countries.

Exhibit 5: Supplier margins and returns are higher than retailer margins and returns²²

Supplier vs Retailer comparison based on reported financial returns



2.1.5. These factors demonstrate that the price comparisons made in the Draft Report are not evidence of a lack of competition in the New Zealand grocery industry and cannot be relied upon as justification for intervention. In fact, after correcting the retailer returns and pricing analysis in the Draft Report, it shows that the key driver for any residual pricing differences is not driven by grocery retailers, but rather other factors. This is not reflected in the Commission's findings nor in the options canvassed in the Draft Report. We request the Commission address the points we have raised in its Final Report (including the points that we had raised prior to the publication of the Draft Report that were not addressed in the Draft Report).

2.2. Supermarket returns in New Zealand do not suggest there is an issue with competition

2.2.1. We do not agree that supermarket returns in New Zealand suggest there is an issue with competition. We also think the way that the Commission is calculating and interpreting our returns is wrong.

2.2.2. We are a low-margin business: Our focus every day is to provide the best prices we can, and this is reflected in our low margins (2.4 cents in every dollar spent at our supermarkets).²³ For every \$1 spent by a customer in a supermarket, we pay 63 cents directly to our suppliers; 19 cents is the cost of running our supermarkets, supply chain and paying our team; 13 cents is GST, and 2 cents is interest and other tax costs. See Exhibit D9 in Part D.

²² These Returns on Capital Employed metrics are calculated using a different methodology to the Commission in the Draft Report. They are based on Orbis database calculations using the standardised formula of (P/L before tax + Interest paid) / (Shareholder funds + non-current liabilities). WWNZ numbers are calculated by applying the same formula to the adjusted financials (post removal of non-grocery items) to enable a like for like comparison. Note: returns are based on closing capital position as of year-end (not average); in all cases margin and returns are based on the latest available financial results (FY20) Source: Orbis, WWNZ adjusted financials.

²³ FY2020.

- 2.2.3. Our margins and returns are lower than those of Woolworths Group in Australia, which operates in a highly competitive market: We are part of the publicly-listed Woolworths Group, so we measure and report a number of comparable financial measures across our New Zealand and Australian businesses. This shows in FY2019 that EBIT margins (New Zealand 4.4%, Australia Food 4.6%), gross profit margins (New Zealand 24.4%, Australia Food 28.7%) and Return on Funds Employed (New Zealand ~9%, Australia Group ~14%) were all lower for WWNZ than Woolworths in Australia.²⁴ Given the Australian market is considered “highly competitive”,²⁵ this means either that our returns are consistent with high levels of competition, or that no meaningful conclusions about competition can be drawn from comparisons of returns.
- 2.2.4. Our margins and returns are lower than other large retailers in New Zealand: While noting the difficulties in comparing businesses (see section 27 in Part D below), our average EBIT margins for 2015 to 2019 (at 4.7%)²⁶ were lower than the average (8.1%) of other publicly listed retailers in New Zealand.²⁷ Similarly, a comparison of the more widely used measure of return, Return on Capital Employed, shows WWNZ (at 9%)²⁸ achieving significantly lower returns (using the same measure) than other major New Zealand retailers such as Hallensteins Glassons (67.9%),²⁹ Briscoes Group (44.3%), and The Warehouse (16.1%).³⁰
- 2.2.5. There are significant issues with the Commission’s comparison of international grocery retailer margins and returns: This includes, not considering the impacts of accounting write-offs and different accounting approaches to calculating gross profit,³¹ and inconsistency in which retailers were included in, or excluded from, the comparison set. Conclusions about competition also cannot be drawn from trends in gross profit given the number of different factors that influence that metric (such as enhanced efficiency).³² These issues are discussed further at paragraph 27.5 in Part

²⁴ Return on Funds Employed is a pre-tax measure of return, calculated as EBIT divided by Average Funds Employed where Funds Employed is Total Assets (excluding deferred tax assets) less Total Liabilities (excluding income tax liabilities, borrowings and lease liabilities).

²⁵ (2019). Bankwest Future of Business: Focus on Supermarkets Report. Retrieved from: <https://www.bankwest.com.au/content/dam/bankwest/documents/business/insights/focus-on-supermarkets-report-2019.pdf>. See also (27 June 2019). USDA: Australia Retail Food sector Report 2019. Retrieved from: https://apps.fas.usda.gov/newgainapi/api/report/downloadreportbyfilename?filename=Retail%20Foods_Canberra_Australia_6-27-2019.pdf, which notes that “the supermarkets industry is one of the most fiercely competitive sectors in Australia.”

²⁶ Average 2016-2019, based on NERA analysis of FactSet financial data for publicly listed NZ retailers.

²⁷ Including Smiths City Group Ltd, The Warehouse Group Ltd, Hallenstein Glassons Holdings Ltd, Briscoe Group Ltd, and Kathmandu Holdings Ltd.

²⁸ These Return on Capital Employed figures are pre-tax, and calculated using a different methodology to that used in the Draft Report.

²⁹ WWNZ understands that Hallensteins Glassons’ Return on Capital Employed is at this level because it has a significant proportion of leased assets, and this was calculated prior to it implementing IFRS 16. Adopting IFRS 16, WWNZ understands Hallensteins Glassons’ Return on Capital Employed is closer to 26%. This further demonstrates WWNZ’s view that excluding leased assets from a firm’s asset base leads to artificially high Return on Capital Employed calculations, and why it is necessary for leased assets to be taken into account (and demonstrates why IFRS16 has been introduced). See paragraphs 27.4 and 27.6 in Part D.

³⁰ Three year average for these other retailers. Armillary Private Capital “Return on Capital Employed - Review of 2019 Returns” / Armillary Private Capital “Return on Capital Employed - Review of 2018 Returns.”

³¹ Woolworths Group, including WWNZ, is one of the few supermarket retailers internationally that does not take into account store and warehousing costs in calculating its “gross profit”, so WWNZ’s gross profit cannot be compared on a “like-for-like” basis with other overseas retailers (that is, as it appears artificially high in comparison to other retailers that adopt different accounting practices).

³² For example, WWNZ has achieved an increase in gross profit margin (while its retail prices have been decreasing in real terms) by focusing on initiatives, such as reducing stock loss, improving product mix, and improving distribution efficiencies via use of our DCs.

D.

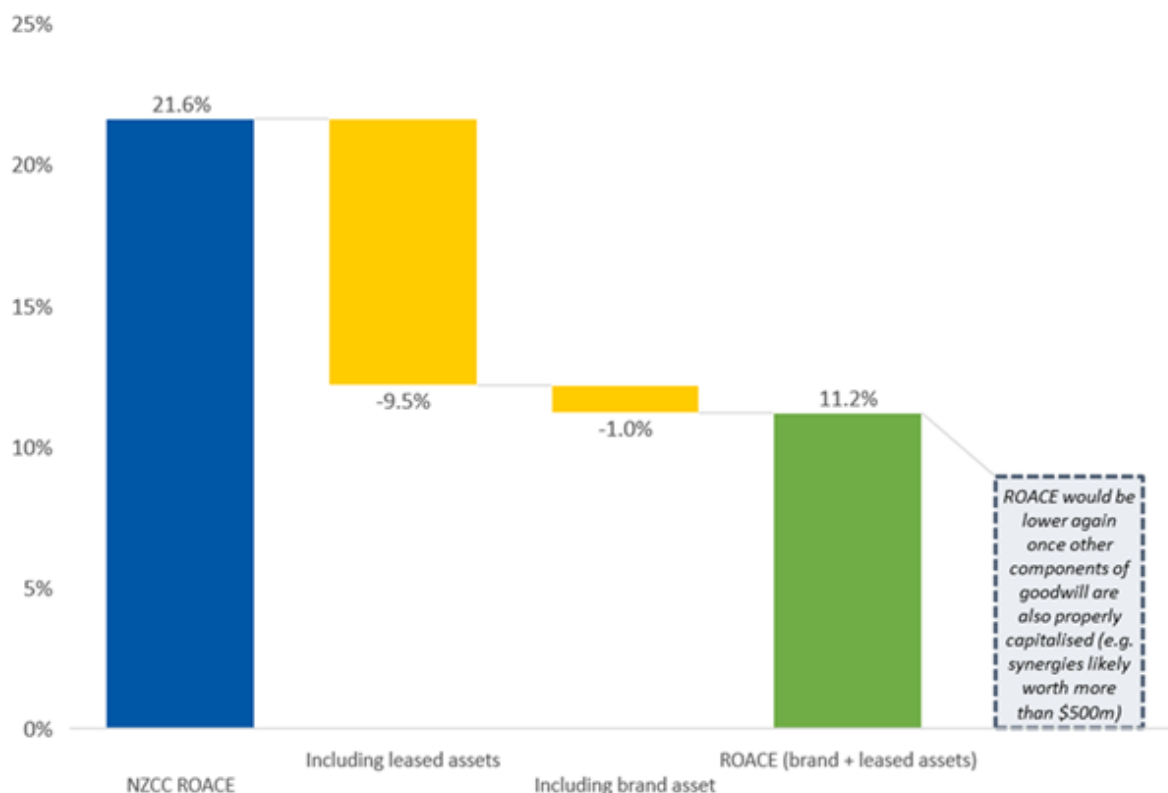
- 2.2.6. The Commission's analysis does not reflect how returns are assessed commercially: WWNZ returns are reported annually as part of the Woolworths Group Annual Report. The calculations are based on the accounts that are prepared in accordance with mandatory New Zealand and international accounting and reporting standards as part of our obligations as a subsidiary of a listed entity. The [] reported return is an accepted measure of the pre-tax return on the capital in the business. The Commission has its own way of looking at returns (Return on Average Capital Employed, a post tax return), but that does not reflect how returns are assessed commercially. This is discussed further at paragraph 27.6 in Part D.
- 2.2.7. The Commission's calculation of our returns is not correct and substantially overstates the results: The Commission's analysis significantly overstates our returns as a result of excluding the investments we have made in several key assets that we use to run our business - namely brand assets and leased assets (it is common for retailers to hold long-term leases for their premises, and those are required by international accounting standards to be treated as capitalised assets on the balance sheet). The Commission's approach does not reflect economic reality, is inconsistent with international accounting standards,³³ and is inconsistent with the Commission's own approach in its Retail Fuel Market Study.³⁴ In our view, the Commission's approach here is fundamentally wrong. Economic analysis by NERA (see **enclosed**) supports our view, as does commentary from financial analysts. We consider that the Commission should correct this, particularly given the Commission's analysis of our returns is so fundamental to its findings. Specifically, even assuming the rest of the Commission's returns analysis is correct (including assuming the Commission's exclusion of goodwill is correct), the exclusion of the leased assets and brands is the difference between our Return on Average Capital Employed being 21.6% (as calculated by the Commission in the Draft Report) or 11.2% (as calculated if our leased assets and brands are taken into account). See Exhibit 6 below. We also do not agree with the Commission's exclusion of other assets that comprise goodwill, including synergies (which, if capitalised, would likely account for more than \$500 million of value), licences, customer contracts, supplier relationships, and transport contracts and networks. These issues are discussed further in paragraph 27.7 in Part D.

³³ IFRS 16.

³⁴ Note that in the Commerce Commission's Fuel Market Study it said:

- It "define[d] the market value of the fuel business as... the market value of the firm's equity... plus the value of debt, the net derivative financial instruments, the value of capitalised leases and deferred tax liabilities."
- "known brand should attract additional customers to the retail sites, regardless of whether it is developed internally or acquired. We therefore include the cost of Z Energy's 2011 rebrand as one of its intangible assets."

Exhibit 6: Cumulative impact on Return on Average Capital Employed of including brands and leased assets³⁵



2.2.8. We do not agree with how the Commission has assessed WACC: The Commission has estimated our post-tax WACC to be 4.6% to 6.1%.³⁶ However, that estimate differs from the WACC, of [], that Woolworths Group calculates and uses for internal business planning and investment purposes for WWNZ. It is important Woolworths Group get it accurate, and they have no incentive to overstate it. We also disagree with the Commission's core thesis that returns in excess of WACC are evidence of a competition issue. To illustrate the point, almost half of all listed and crown entities in New Zealand achieve returns greater than WACC.³⁷ WACC is, in fact, a minimum benchmark for firms to be sustainable over the long-term and to attract capital to enable continued investment in products and services that benefit end-consumers (such as the hundreds of millions of dollars [] of investment we have underway or planned in the next two years in building new stores, upgrading existing stores, strengthening our supply chain and other innovation and investments), as well as the significant investments we have made, and continue to make, in our online, digital, and e-commerce capabilities (such as our investments in three dedicated eStores, New Zealand's first semi-automated fulfillment units, Pick Up, Drive Through, and Delivery experience innovations, rollout of eLockers to [] stores by the end of this calendar year and launch of robotic temperature-controlled grocery collection lockers, and enhancements to our mobile app, including in-app transactional capability, digital Onecards, eReceipts, and store aisle-locator product

³⁵ NERA analysis, Commerce Commission WWNZ ROACE Model.

³⁶ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [3.20].

³⁷ Armillary Private Capital "Return on Capital Employed - Review of 2019 Returns" / Armillary Private Capital "Return on Capital Employed - Review of 2018 Returns."

finder). []

2.2.9. We do not agree with the Commission's interpretation of our business cases: The Draft Report includes a preliminary finding that we have an expectation of excess returns based on the Commission's review of some of our business cases for new investments. However, that is not a correct interpretation of those business cases. The problem stems from the fact that the Commission only asked us for business case materials in relation to a certain type of investment - namely, investments in new supermarkets, refurbished / expanded supermarkets, or online shopping. That is only a small subset of the investments that we make, and they are investments in the consumer-facing (that is, revenue-generating) parts of our business (that is, "growth" investments). Investments in such "growth" projects make up only about [] of our capital investment in most years. In any given year there is significant capital expenditure on other "stay in business" items, and a large proportion of that is not expected to make any direct material return. Examples include seismic strengthening of buildings, replacement of store or warehouse equipment, IT systems, and investments in health and safety initiatives for our people. Of course, we cannot have the consumer-facing part of our business without those important "stay in business" investments, but they do not generate returns themselves. As a result, the financial return across WWNZ's total capital expenditure will be significantly lower than the range referred to in the Draft Report. It is not appropriate to only assess individual business cases for "growth" investments, as "growth" business cases need to achieve returns above the cost of capital to enable the business (on a total basis) to at a minimum cover WACC.

2.2.10. Many other factors, unrelated to competition, influence returns - and the Commission's approach, which is not adopted elsewhere, systematically overstates returns:

2.2.10.1. Differences in accounting treatment (including accruals, depreciation charges, intangible assets, asset valuations, write-downs and impairments), the age of assets, and efficiency (that is, a more efficient business will have higher returns) will all have a significant impact on the calculation of returns. In particular, the Australian Competition and Consumer Commission (**ACCC**) has recognised that the age of assets, and how they have been depreciated for accounting purposes, is a significant factor in determining the outcome of returns analysis³⁸ - particularly, for businesses such as supermarkets that often have heavily depreciated assets.

2.2.10.2. Given WWNZ has a number of long-lived, heavily depreciated assets, this is inevitably a significant driver of the calculation of WWNZ's returns. Indeed, whatever a business' pricing or profits might have been, the Commission's approach to calculating returns will *a/ways* find returns in excess of WACC for a business with long-lived assets that have already been heavily depreciated (such as WWNZ). See the **enclosed** report by NERA.

³⁸ "The ACCC agrees that care is needed when interpreting [returns analysis] as it is heavily influenced by the value of the underlying assets and the extent of depreciation." See ACCC. Report of the ACCC inquiry into the competitiveness of retail prices for standard groceries. (July 2008). At page 111.

2.2.10.3. For these reasons, in its grocery market study, the ACCC concluded that “*significant conclusions cannot be drawn*” from returns analysis such as analysis of Return on Funds Employed, and acknowledged concerns that they could be “misleading”.³⁹ However, in contrast to the ACCC, the Commission’s Draft Report does not apply such caution.⁴⁰ Instead the Draft Report uses its returns analysis to justify a range of findings, and canvas a range of extreme options. In our view, not only is significant caution required in interpreting returns analysis, but the Commission’s approach to returns analysis is fundamentally incorrect (see paragraph 2.2.7 above) and appears predestined, in our view, to find returns that exceed WACC in most industries that it analyses using this approach.

2.3. Despite the Draft Report’s narrow framing of the market, the New Zealand retail grocery sector is intensely competitive, and new entry is both already here and further new entry is inevitable

2.3.1. We stand by the evidence presented in our Initial Submission that the New Zealand retail grocery sector is both dynamic and intensely competitive, and we consider that the Draft Report does not take a sufficiently forward-looking view of competitive dynamics.⁴¹ As a result of that, the Draft Report has drawn conclusions that do not reflect our experience as a participant in the retail grocery market. Most notably in relation to the following:

2.3.2. The Draft Report excludes almost half of grocery sales from its frame of reference:

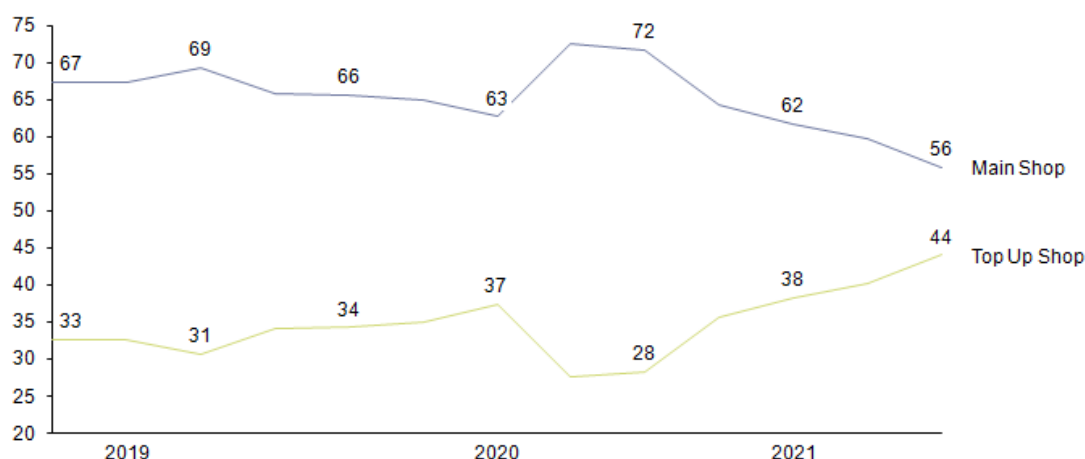
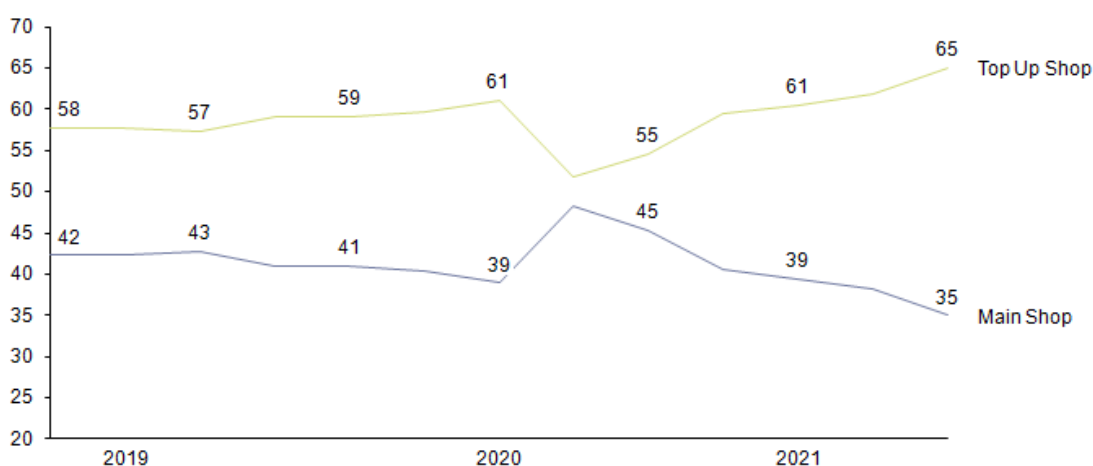
2.3.2.1. The Draft Report’s focus on “the main shop” (and the corresponding lack of consideration of other shopping missions) is outdated and does not capture the full competitive landscape. In 2021, “non-main shop” shopping missions are a critical and increasing area of grocery market competition, consistent with accelerating convenience trends outlined in our Initial Submission.

2.3.2.2. To illustrate this further, [] data shows that as at July 2021 only 35% of grocery shopping missions in New Zealand were for a “main shop” (down 7% from 3 years ago), representing just 56% of total supermarket sales (down 11% from 3 years ago). That means that almost two-thirds of all missions (and almost half of all expenditure), relate to shopping trips that the Draft Report does not regard as relevant (and the decline in “main shop” missions would be even starker if it were not for an increase in larger COVID-19 related shopping missions last year).

³⁹ ACCC. Report of the ACCC inquiry into the competitiveness of retail prices for standard groceries. (July 2008). At page 111.

⁴⁰ The statement in the Draft Report (at [C42]) that the ACCC study “did not state why they had not used [returns analysis]” is incorrect. As noted, the ACCC acknowledged the concerns raised that such analysis could be “misleading” and, therefore, that “significant conclusions cannot be drawn” from returns analysis. We ask that this be addressed in the Final Report.

⁴¹ The ordinary competition law approach required by the courts is to take a “forward-looking” view of competitive dynamics. See: *New Zealand Bus Ltd v Commerce Commission* [2007] NZCA 502 at [237]. See also Commerce Commission “Mergers and acquisitions guidelines (July 2019) at [2.35] in which the Commission notes that it takes a “pragmatic and commercial assessment of what is likely to occur in the future with and without the merger”.

Exhibit 7: Consumer expenditure by different grocery shopping mission type (%)*Exhibit 8: Consumer shopping trips by grocery shopping mission type (%)*

2.3.3. Even within the narrowly framed market, competition is strong including on price: The Draft Report takes the view that innovation in the New Zealand grocery sector is not directed at price and that “food discounter type business model innovations such as offered by Aldi overseas, have not occurred in New Zealand.”⁴² We disagree. If it were operating in overseas markets, PAK’nSAVE (with unlined interiors, concrete floors, cardboard boxes in the retail area, customers asked to pack their own bags and by-line “our policy: NZ’s lowest food prices”), would be classified as exactly that type of “food discount ... no frills” competitor. In fact it operates that model across a wider-range of branded and private label products than most “food discount ... no frills” grocery retailers internationally. Competition is also fierce across non-price dimensions including shopping experience, product range and service levels (as evidenced by a number of world leading innovations - see section 29 in Part D).

⁴² Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [3.145].

- 2.3.4. The Draft Report excludes and marginalises online groceries, despite rapidly changing relevance: The Draft Report's focus on "bricks-and-mortar" retailers, to the exclusion of online grocery sales, does not capture the full competitive landscape or take a forward-looking view. Countdown's online penetration continues to rapidly grow, having increased from 3% of total sales in FY2014 to over 12% in FY2021, and []⁴³ (that is, an increase of over 400% [] from FY2014 to FY2021). This customer need is such that the size of Countdown's current online business is already equivalent to over 20 physical supermarkets, and by the end of FY2023 would be as large as more than [] supermarkets. This is plainly where a significant and ever-increasing number of Kiwi consumers are choosing to purchase their groceries (as evidenced by the plethora of new online competitors). Excluding online retailers ignores that online retailing will increasingly become the key area of competition and will provide opportunities for new businesses and innovative business models.
- 2.3.5. New retail entry has occurred across both main and non-main shops, and the potential for further entry and expansion is real: The Draft Report takes the view that there has not been any new entry in grocery retailing in New Zealand in the last decade, and there is unlikely to be further new entry.⁴⁴ Again, we disagree. There is a range of existing grocery competitors operating differentiated business models - such as Farro Fresh, My Food Bag (which has launched an online grocery offering),⁴⁵ HelloFresh (which is increasingly expanding into online groceries overseas), and The Honest Grocer. Even beyond those competitors, the reality is that:
- 2.3.5.1. Costco is entering New Zealand: Costco is the second largest "bricks-and-mortar" food / grocery retailer in the world, and has market capitalisation more than five times larger than the Woolworths Group. Costco will soon have stores in New Zealand with catchments that cover ~40% of the New Zealand population⁴⁶ (and in Australia it has launched online shopping and delivery, which would expand its coverage further if also launched in New Zealand).⁴⁷ Each Costco store has, on average, the floor space of six Countdown stores,⁴⁸ so expansion by Costco to three stores would have the equivalent floor space of 18 Countdown stores. It is difficult to imagine a new entrant that is better resourced and qualified to compete, let alone one with such a clear price proposition.
- 2.3.5.2. The Warehouse is increasingly expanding into grocery products, and has more than 90 stores New Zealand wide (as well as TheMarket online platform). While publicly stating it has intentions to become "the Amazon of New Zealand",⁴⁹ The Warehouse has downplayed their capabilities and

⁴³ Measured prior to the latest August 2021 Level 4 lockdown.

⁴⁴ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [6.25.2] and [6.26].

⁴⁵ (5 August 2021). My Food Bag expands into groceries, targeting growth from \$37b retail food sector. The New Zealand Herald. Retrieved from: <https://www.nzherald.co.nz/business/my-food-bag-expands-into-groceries-targeting-growth-from-37b-retail-food-sector/UDZ6EOYNJQY6BOFJP2SIDWSGOE/>

⁴⁶ Costco is said to be "also actively looking for sites in Christchurch and Wellington", in addition to the Auckland site that is currently in development. See:

<https://www.odt.co.nz/star-news/star-business/how-much-you-could-save-when-costco-makes-nz-debut>

⁴⁷ (12 February 2020). Costco has announced it will launch members-only online shopping and delivery in Australia. Business Insider. Retrieved from: <https://www.businessinsider.com.au/costco-delivery-2020-2>

⁴⁸ WWNZ understands that, on average, a Costco store has floor space of 13,470 sqm.

⁴⁹ (2 August 2019) New market realities and The Warehouse Group's TheMarket. The Register. Retrieved from: <https://theregister.co.nz/2019/08/02/new-market-realities-and-warehouse-groups-themarket/>

ambitions in grocery and seemingly exaggerated the hurdles to success through their submissions to the Commission. The Warehouse's push into groceries is highly observable, as illustrated further at paragraph 30.6 in Part D.

2.3.5.3. Aldi is an inevitable entrant: The prospect of Aldi's entry into New Zealand informs our strategic thinking. It has a long history of denying plans to enter a new territory, before then doing just that.⁵⁰ We consider its expansion into New Zealand is only a matter of time. Evidence for this includes that:

2.3.5.3.1. Aldi has rapidly expanded in Australia and is now approaching its reported target.

2.3.5.3.2. Aldi's store location and footprint requirements are broadly similar to Chemist Warehouse - and despite only launching in New Zealand in 2017, Chemist Warehouse is expected to reach 35 stores here by the end of the year⁵¹ (with plans to expand to 70 stores nationwide).⁵² This demonstrates that Aldi achieving the Draft Report's cited threshold of 10 stores to enter the New Zealand market would be readily achievable.⁵³

2.3.5.4. Access to an independent wholesaler is not a barrier to entry or expansion: We disagree that new entry is reliant on the introduction of an "independent" wholesaler. This has not been a prerequisite for The Warehouse's existing grocery offering, for Costco's imminent entry, or for the success of My Food Bag, HelloFresh, and Farro Fresh, each of whom have formed direct relationships with suppliers.⁵⁴

⁵⁰ We note Aldi made statements in September 2009 and October 2012 denying plans to expand to Western Australia before announcing its expansion into Western Australia in February 2013. See for example:

- (19 September 2009). Reforms not enough to attract discount supermarket to WA. WA Today. Retrieved from: <https://www.watoday.com.au/national/western-australia/reforms-not-enough-to-attract-discount-supermarket-to-wa-20090918-fv7a.html>
- (25 October 2012). ALDI Continues to grow along the east coast. Australian Food News. Retrieved from: <https://www.ausfoodnews.com.au/2012/10/25/aldi-continues-to-grow-along-the-east-coast.html>
- (12 February 2013). Western Australia and South Australia's cries for ALDI have been heard. Australian Food News. Retrieved from: <https://www.ausfoodnews.com.au/2013/02/12/western-australia-and-south-australia%E2%80%99s-cries-for-aldi-have-been-heard.html>

⁵¹ (29 March 2021). Chemist Warehouse looks to regional areas for NZ growth. Inside Retail. Retrieved from: <https://insideretail.com.au/business/chemist-warehouse-looks-to-regional-areas-for-nz-growth-202103>

⁵² (5 March 2020). Australian pharmacy giant Chemist Warehouse to open in Christchurch. Stuff. Retrieved from: <https://www.stuff.co.nz/business/120003495/australian-pharmacy-giant-chemist-warehouse-to-open-in-christchurch>

⁵³ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [6.157].

⁵⁴ Costco is also expected to become a significant wholesaler in its own right in New Zealand. For example, in Australia 30% of its sales are estimated to be to business customers.

2.4. The New Zealand grocery sector is highly innovative, with high levels of online retailing, and significant investments in stores and supply chains

2.4.1. Our levels of innovation are high and in line with those of global leaders: The Draft Report states that competition “provide[s] strong incentives for innovation”.⁵⁵ We agree, and our view is there has been, and continues to be, significant investment in innovation in the New Zealand retail grocery market. We have already implemented almost all of the examples of “international innovation” that the Commission’s Draft Report cited as missing from New Zealand (see Exhibit D28 in Part D). The suggestion that there is a “slower pace of innovation by grocery retailers in New Zealand”⁵⁶ is not correct.⁵⁷ Other examples of our leading-edge innovations include (among many others):

2.4.1.1. New Zealand’s first semi-automated online fulfillment units (including just the second in the Southern Hemisphere, and ninth in the world).

2.4.1.2. A world-first personalised online mailer.⁵⁸

2.4.1.3. A dispensing robot for greater speed and accuracy in our in-store pharmacy, and an in-store grocery robot to identify spills, hazards, and gaps in the shelves.

2.4.1.4. Automated self-serve frozen, fresh and dry eLockers in the car parks of 18 stores (and rapidly growing).

2.4.1.5. Contactless “Scan&Go” service where hi-tech scales can detect what our customers are buying so they can skip the checkout.

2.4.1.6. Extensive in-store innovations including: dedicated health-foods aisles, early adoption of self-checkouts, electronic shelf labels, digital Onecard scanners, free fruit for kids, app-assisted shopping, eReceipts, and NZ’s first Green Star rated supermarket.

2.4.2. We are a leader in online grocery retailing: New Zealand’s level of online grocery penetration is high by international standards, and even higher once adjusted for population density. The Draft Report put New Zealand’s overall online grocery penetration at 5.7% of total sales (nationally), and suggested (in our view, incorrectly) this is “comparatively low when compared to other countries.”⁵⁹ To the contrary, this puts New Zealand on par with Australia and Sweden, and already significantly higher than the US, Germany, Italy and Spain. Comparisons to countries like China, South

⁵⁵ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [6.25.2] and [3.139].

⁵⁶ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [3.165].

⁵⁷ It is also not accurate for the Draft Report to cite “one off” innovations in overseas markets as evidence that, compared to those overseas markets, innovations in New Zealand “have not yet been adopted or implemented in any consistent or widespread manner across retail grocery stores”. For example, we understand that the “living herb wall” and pick and mix bar dog treats is only in one small format Coles Local store in St Kilda, so is not an example of “consistent or widespread” innovation compared to New Zealand. We also note that the “living herb wall” was understood to be a failure, and was withdrawn from that store.

⁵⁸ See <https://www.digitasaffinity.id/case-studies/mycountdown/>.

⁵⁹ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [3.154]. Further, at [2.62] the Draft Report also states that it is unclear whether the increase in online shopping “will continue in future” (that is, beyond last year’s COVID-19 lockdowns). In our view, that data is clear that the increase in online shopping will continue to grow. Our online penetration has grown rapidly to be in excess of 12%, and is continuing to grow [].

Korea and the UK also need to adjust for population density (which is a key determinant to feasibility and uptake of online retailing). After taking this into account, it is clear that New Zealand is among global leaders, and at Countdown specifically, we have more than 12% online penetration [], which is at world-leading levels. While Foodstuffs South Island (**FSSI**), in particular, may be a late adopter, this is most likely due to the complexities of its cooperative owner-operated structure, as opposed to any lack of competitive imperative (a dynamic also observed overseas with owner-operated banners, as in the case of the Metcash supplied IGA banner in Australia, which only launched a national online grocery offering in 2020).⁶⁰

2.4.3. We invest extensively in our stores to provide attractive (and increasingly sustainable) shopping environments: We invest over [] per annum in building new stores, upgrading and innovating our existing stores, and launching new formats. We have a large pipeline of store renewals planned [(up to [] new stores and [] renewals between FY2022 to FY2024)], including opening more of our small-format Metro stores to meet customers' demand for convenience, and accelerating drive up, drive-through and eLocker rollout. Our newest stores also include a number of innovative features to reflect our commitment to environmental sustainability - including solar panels, LED lighting, water-saving taps, EV chargers for customer cars, bike parks for customers, and electric online delivery trucks. We recently opened New Zealand's first Green Star-rated supermarket, and are committed to all new property developments achieving a 4 Green Star rating, and by 2025 we aim to have a 5 Green Star-rating minimum standard.

2.4.4. We invest extensively to provide New Zealand an efficient and resilient supply chain:

2.4.4.1. We have made, and continue to make, significant investments in our integrated supply chain and logistics capabilities. We have a number of significant investments in logistics projects currently underway or approaching completion with an estimated capital investment of approximately [] (from both WWNZ and our partners). This includes:

2.4.4.1.1. Developing a new purpose-built 38,000 sqm distribution centre in Palmerston North to service the lower North Island. This \$100 million project has opened from August 2021, and will deliver 70 new jobs, a number of energy and water efficiency initiatives (for example, rainwater harvesting), and significantly improved on-shelf-availability, service levels, and supply chain resilience for the Lower North Island by holding 7,000 SKUs (compared to 1,700 SKUs previously).

2.4.4.1.2. Partnering with Hilton Food Group, to establish a brand new, state-of-the-art, \$100 million meat processing plant in Auckland, which opened in July 2021. This includes innovative new products (including ready meal SKUs), new packaging (for example, sealed fresh packaging that improves shelf-life and product quality), and new distribution (for example, new crates, robotic sorting, and co-distribution with fresh produce to drive efficiencies).

⁶⁰ (21 May 2020). IGA rolls out national online grocery service. InsideRetail. Retrieved from: <https://insideretail.com.au/news/iga-rolls-out-national-online-grocery-service-202005>

2.4.4.1.3. Partnering with Americold to establish a \$65 million expanded temperature-controlled warehousing facility in Auckland which opened in July 2021 (and will also support wider temperature-controlled capacity into the market).

2.4.4.1.4. Developing a new state-of-the-art 20,000 sqm produce distribution centre in Auckland (“go-live” in FY2022) to help service all of Countdown’s North Island stores with fresh fruit and vegetables direct from local growers. This involved total capital investment of [], including [] from WWNZ [], and includes improved cold chain management to deliver better quality outcomes for customers.

2.4.4.1.5. [].

2.4.4.2. We make these investments to ensure our network can meet our future supply chain requirements and efficiently meet our customers’ needs. Consumers benefit significantly from these investments. The enhanced efficiencies we have achieved have helped us to reduce our retail prices (in real terms) over the last decade, deliver improved service and quality outcomes, and provide us with the capability and resilience to deal with unexpected shocks to either supply or demand. They also help mitigate supply chain cost increases that would otherwise occur (estimated at [] over the next 6 to 7 years).

2.4.4.3. Our response to the challenges presented by COVID-19 demonstrates this. In times of crisis we are able to rapidly adapt, in an integrated “all of system” way, to adjust the allocation of product to different stores (for example, priority communities), to optimise stock levels and deliveries across our network, to smooth demand to reduce shortfalls (for example, imposing product limits in stores), to alter our store opening hours (to allow more time for replenishment), to impose customer purchase limits (to best enable availability for all our customers), to manage distribution and retail channels to optimise supply (for example, partnering with suppliers to allow direct-to-store delivery for some categories, or quickly opening online-only fulfilment centres) - all to improve outcomes and grocery access for Kiwis in an incredibly challenging environment. In addition, within a very short period of time in March and April 2020, we were able to rapidly add scale to our online grocery capacity (a 60% expansion in online shopping capacity for Countdown within a matter of weeks), create a priority access system via Countdown’s website (to enable vulnerable customers to shop online), launch a pilot e-queue system (to allow people to wait in their cars for in-store shopping), and launch an online offering for the Supervalu / FreshChoice stores.

2.4.5. See further details on the points above in section 33 in Part D.

2.5. Other areas where we have a different view to the Commission

2.5.1. There are a number of other areas in the Draft Report where we have a different view to the Commission - as set out in **Part D**.

3. Positive changes to retailer practices that we support

- 3.1. While we do not agree with all of the preliminary findings in the Draft Report, we acknowledge that there are a number of areas where changes could help the sector improve. Below, we outline our support for a number of changes to industry practices that the Commission has put forward, which we agree will result in benefits for consumers and suppliers.
- 3.2. **Mandatory Grocery Code:** We support the introduction of a grocery code that includes checks and balances to help improve relationships between retailers and suppliers; provides assurances that suppliers can speak up safely; and provides a trusted and effective dispute resolution mechanism. While we would voluntarily sign-up to such a code, to ensure it achieves the best results across the entire industry, we consider that any code should be mandatory.
- 3.3. **Mandatory Unit Pricing:** We support the introduction of a mandatory unit pricing code that requires prices by standard units of measure (for example, by volume, weight, or number) to be prominently displayed for all grocery items. In our stores, we mostly provide unit pricing information for each product, and making it mandatory across all retailers would ensure consumers receive consistent 'price per unit' information to help them to make price and value comparisons.
- 3.4. **Further simplification of pricing and promotions:** We are open to working with the Commission to understand how we can provide simpler and clearer pricing and promotions for our customers. For example:
 - 3.4.1. We would welcome the opportunity to work with the Commission to develop clear industry-specific guidelines on promotions and "was / now" pricing so that a fair and consistent approach can be adopted.
 - 3.4.2. If the Commission thought it would be beneficial for consumers, while our retail prices are already publicly available in-store and on our website, we would also be open to discussing the possibility of providing a regular access feed to retail prices to enable the development of independent price comparison services (similar to Consumer NZ's Powerswitch website in the electricity sector).
- 3.5. **Further simplification of loyalty programme terms:** We are open to working with the Commission on how we can provide better clarity on the terms and operation of our loyalty programmes.
- 3.6. **Appointment of a grocery ombudsman or adjudicator:** We support the formation of a Government-appointed grocery ombudsman or adjudicator to provide oversight and independence in implementing and monitoring compliance with these changes.
- 3.7. We believe that these changes, combined with the imminent introduction of prohibitions on unconscionable conduct and unfair contract terms (**UCT**) will further enhance the compliance frameworks and pricing practices of the sector for the benefit of consumers and suppliers.
- 3.8. See **Part A** for our views on how these changes could be framed to achieve the best results for New Zealand.

4. Changes to assist further new entry and expansion that we support

- 4.1. As stated, in our view New Zealand's retail grocery market is already competitive, and is becoming more so, organically, and without intervention.
- 4.2. We do not, therefore, consider that what would be internationally unprecedented regulatory intervention would be of benefit to New Zealand (for example, forced separations, divestments and regulated access regimes).
- 4.3. The Draft Report acknowledges that no cost / benefit analysis has been conducted on these options, and that they carry significant risk of "lost efficiencies", "costs", and "distortion of investment incentives" (including beyond the grocery market).⁶¹ We share these concerns. Our view is such interventions could easily lead to a number of unintended consequences, for example they would:
 - 4.3.1. undermine efficiencies (particularly problematic for New Zealand given we are already a very small market with geographical challenges), product traceability, and supply chain resilience benefits to consumers from vertical integration;
 - 4.3.2. risk market distortion (for example, would Costco, the world's second-largest "bricks-and-mortar" retailer, also be subject to regulation, or just WWNZ, FSSI, and FSNI?);
 - 4.3.3. create significant costs and complexity - in regulatory design, implementation, and ongoing monitoring. Globally there is no precedent of any intervention in, or economic regulation of, grocery markets of this nature. This means there would be significant design costs in developing any regime, and significant ongoing monitoring and administration costs in trying to monitor outcomes in a market with multitudes of competitors operating differentiated business models to compete across thousands of products;
 - 4.3.4. re-allocate assets / value to questionable ends - for example, by encouraging other grocery retailers to be 'reliant' on WWNZ's, FSNI's, and FSSI's assets and supply chains through a regulatory framework, rather than incentivising them to invest in their own assets and supply chains to be true independent competitors. There is also the question of how a new grocery retailer 'constructed' from an arbitrary combination of divested assets could be expected to efficiently compete (instead of encouraging organic investment and growth in an efficient manner);
 - 4.3.5. undermine incentives to invest - both in the New Zealand grocery sector, and the broader economy; and
 - 4.3.6. likely (given everything above) ultimately lead to higher prices and poorer outcomes for consumers.
- 4.4. For these reasons, we recommend the Commission focus on options that:
 - 4.4.1. remove impediments to entry of new participants or further expansion of existing participants, without undermining the scale, efficiencies and investments of existing grocery retailers; and

⁶¹ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [9.64].

- 4.4.2. best enable the entry and expansion of competitors that are ultimately truly independent of (and not reliant on) WWNZ, FSNI, FSSI's assets or businesses.
- 4.5. The following are measures we think would achieve the above, subject to detailed design:
- 4.5.1. Law change to make exclusivity / "no supermarket" provisions in leases and land covenants unenforceable: While there are legitimate and pro-competitive reasons for land covenants and exclusive leases provision, we would support a regime that makes such covenants and lease provisions unenforceable (except in limited circumstances where required to enable investment in a new supermarket for a defined period or in other circumstances where necessary for the operation of a supermarket on a particular site).
 - 4.5.2. Law change to restrict exclusivity provisions in standard supply contracts with grocery suppliers: We would support a regime that makes exclusivity provisions in supplier contracts unenforceable except where they are reasonably necessary for legitimate business purposes, such as where they have been included in integrated (non-standard) supply relationships (for example, where the retailer and supplier have jointly invested significantly in product development, manufacturing facilities, or have jointly developed private label products or intellectual property).
 - 4.5.3. Law change to make "best price" provisions in supply contracts with grocery suppliers unenforceable: We would support this change.
 - 4.5.4. Law change to New Zealand's planning regulations to assist in entry and development of new retail grocery sites: We agree with the Commission that the RMA and consenting processes for new grocery sites is lengthy and costly. We would support changes to New Zealand's planning and consenting regulations to assist entry and development of new retail grocery sites.
 - 4.5.5. Law changes to the OIA to lower the regulatory impediments to entry / expansion by "overseas" supermarket operators such as Costco and Aldi: It would benefit competition if the OIA were amended to level the playing field between domestic and overseas retailers. Such an amendment would allow grocery retailers to obtain general class-based exemptions for the development of grocery stores or distribution centres, or to allow for longer periods on standing consents for residential land.
 - 4.5.6. Assisting (or authorising) the formation of joint buying groups by independent retailers: We would support steps to assist smaller grocery retailers to form joint buying groups to bargain collectively with suppliers. This would enable smaller retailers to achieve better economies of scale in a way that is independent of WWNZ, FSNI, and FSSI's businesses, and without risking complex regulation and the addition of costs and inefficiencies to the system.
- 4.6. See **Part B** for our views on how these changes could be framed to achieve the best results for New Zealand.

5. We have an open mind to voluntary wholesale supply over time

- 5.1. The measures outlined in Section 4 above, if implemented, would accelerate the entry of new competition. For these reasons, in our view, no other interventions are required. If, however,

following the conclusion of the Market Study and sufficient passage of time to implement and assess the impact of the other options we support, there is a view that additional wholesale supply would also be of benefit, then we are open to discussion on the merits of voluntary wholesale supply.

- 5.2. While there are complexities (and costs) to work through in determining the detail of what such arrangements might involve (requiring considerably more time than the six weeks we have had since the Draft Report), in principle we think wholesale supply is potentially feasible for WWNZ (and presumably for FSNi and FSSI too).
- 5.3. In terms of complexities, our assets and grocery supply chain are not currently set up for third-party wholesale. They are set up to support a vertically integrated retail business (including our own Countdown outlets and our franchised outlets). While the Draft Report states we “already have the systems in place to provide wholesale grocery supply” to other retailers,⁶² this is not the case. Significant system and process overhaul and investment would be required. In addition:
 - 5.3.1. At certain points of the year, our supply chains are already at capacity (for example, at Christmas and Easter time, and during surges in demand such as COVID-19 events). For example, in FY2019, across our Auckland Regional Distribution Centre and Auckland National Distribution Centre []. In FY2020 [].
 - 5.3.2. Our supply contracts with suppliers are predicated on us being a retailer (for example, our buying terms envisage us, or our franchisees, activating retail promotions).
- 5.4. Nevertheless, as noted above, if following the conclusion of the Market Study and sufficient passage of time to implement and assess the impact of the other options we support, there is a remaining view that additional wholesale supply would also be of benefit, we would be open to negotiating competitive commercial wholesale arrangements with other retailers. This would require enough lead-in time, as well as the support from our suppliers to amend our buying terms to reflect a wholesale business.
- 5.5. In terms of scope, priority could be given to the type of products the Commission has concerns with not currently being wholesaled by independent wholesalers (for example, packaged groceries),⁶³ and to retailers that fall within the definition of the types of retailers that the Commission has indicated it wants to see emerge as new competitors (for example, “full shop” bricks-and-mortar retailers).

⁶² Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [9.40].

⁶³ The Draft Report noted that options for independent wholesale supply to independent retailers already exist for meat and produce and some imported products (see paragraph 6.127 of the Draft Report). While the Draft Report cited examples such as T&G Fresh and MG Marketing (in fresh produce), the wholesalers listed on the Beef+Lamb New Zealand Website (in meat), and AB International, Acorn Group, Tai Ping, Asian Savour (in imported products), the Draft Report should have also specifically cited that a number of other products are typically supplied by suppliers through a “direct store delivery” (DSD) model, whereby the supplier picks store specific orders and deliver directly to stores - including to numerous supermarkets, service stations, convenience stores, and dairies. The DSD model is often used for products with shorter shelf life (such as bread, milk, and meat) and, therefore, such products do not use or rely on the grocery retailer’s supply chain. Therefore, even taking the Draft Report’s preliminary finding that entry by new grocery retailers is dependent on a grocery wholesaler (which we do not consider is correct), the Draft Report’s preliminary finding is the potential “gap” in relation to wholesaling is limited to long-life packaged products. Therefore, even adopting the Draft Report’s preliminary finding, we could not see a need for WWNZ to enter into commercial wholesale arrangements with other retailers in relation to such products - i.e. fresh produce, meat, imported products, milk, bread, or other DSD products that already catered for by a large number of other wholesalers and suppliers with their own distribution networks.

- 5.6. We consider it would be reasonable to expect those retailers to also need to meet certain minimum service levels and viability requirements. For example, minimum order volumes, order forecasting, health and safety, and other important considerations.
- 5.7. In exploring the option of voluntary supply, it is critical we emphasise that it would not be as simple as “flicking a switch”. Significant investment and adequate lead-in time would be required to build and scale the capability required.⁶⁴
- 5.8. While these costs should not be underestimated, we are clear that if the Commission or Government ultimately considers that further wholesale supply is required, the option of voluntary supply would be a far better alternative for WWNZ, the sector, consumers and taxpayers than other more significant regulatory options canvassed. As such, we retain an open mind and can explore further with the Commission or Government if necessary.
- 5.9. See **Part C** for our views on the options for wholesale access.

6. Concluding comments

- 6.1. We know this Market Study, and the outcome of it, is important to New Zealanders and has the potential to impact our business. For both these reasons we want to help the Commission to ensure its conclusions are sound, and that any recommendations deliver benefits for Kiwi consumers and the country as a whole.
- 6.2. We have highlighted the key areas where we disagree with the Commission, and we have also outlined the options we consider would best help achieve the Commission’s objectives - namely:
- 6.2.1. introduction of a mandatory grocery code and mandatory unit pricing code;
 - 6.2.2. further simplification of pricing, promotions, and loyalty programme terms;
 - 6.2.3. appointment of a grocery ombudsman or adjudicator;
 - 6.2.4. law change to make exclusivity / “no supermarket” provisions in leases and land covenants unenforceable;
 - 6.2.5. law change to restrict exclusivity and “best price” provisions in standard supply contracts with grocery suppliers;
 - 6.2.6. changes to New Zealand’s planning, RMA, and OIA regulations to assist in entry and development of new retail grocery sites; and
 - 6.2.7. assisting (or authorising) the formation of joint buying groups by independent retailers.
- 6.3. Our view is that these measures would, if implemented, best meet those objectives and further accelerate the entry and expansion of new competition.
- 6.4. If however, following the conclusion of the Market Study and a sufficient passage of time to implement and assess the impact of these measures, the Commission or Government considers that other steps are also necessary, we have an open mind to voluntarily

⁶⁴ [].

commencing commercial wholesale arrangements with other independent retailers (subject to working through the complexity of such a change for our business).

- 6.5. In our view, more interventionist regulatory options are not only unprecedented internationally, they carry real costs and high risks of unintended consequence. It is likely to be the Kiwi consumer and taxpayer who ultimately bear that cost, and therefore it's our view that other actions should be considered first.

Part A: Changes to retailer practices that we support

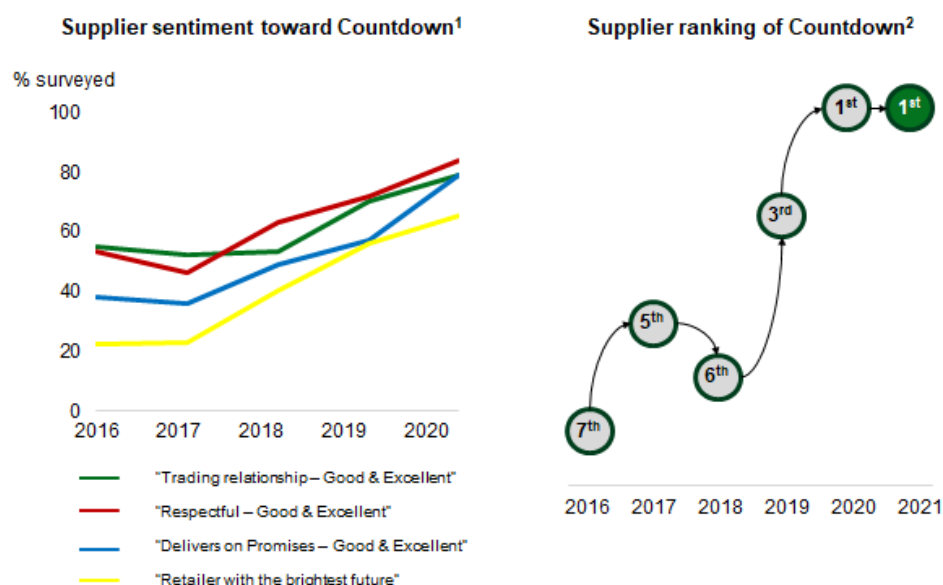
We share the Commission's view that there are areas where measures can be put in place to help the sector improve and we are open to supporting a number of changes to industry practice.

We set out the detail below on how these changes could be framed to achieve the best outcomes.

7. We support the introduction of a mandatory grocery code of conduct

7.1. The Commission found that “many suppliers have good relationships with the retailers they supply”,⁶⁵ and we are proud of the fact that suppliers have rated Countdown as the number one grocery retailer to deal with in New Zealand in both of the most recent major grocery industry surveys.⁶⁶ - see Exhibit A1 below.

Exhibit A1: WWNZ Supplier Sentiment Retailer Scorecard and WWNZ Advantage Insights retailer performance as assessed by suppliers (2016 to 2020-21)⁶⁷



7.2. While we have worked hard on forming positive, enduring and mutually beneficial relationships with our suppliers, there is always room for improvement and we support the introduction of a mandatory grocery code (**Grocery Code**) to supplement our own Supplier Charter. We would work constructively with the Government on drafting and implementation to ensure any Code is effective, pragmatic, and balanced.

7.3. If a Code was a recommendation, our view is that Australia's Competition and Consumer (Industry Codes Food and Grocery) Regulation 2015 (**Australian Grocery Code**) provides a carefully considered blueprint from which to begin, and includes a robust set of checks and

⁶⁵ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [8.73].

⁶⁶ Nielsen Retail Barometer. Advantage Insights' Report. See also Figure 8.2 of the Draft Report.

⁶⁷ Nielsen Retail Barometer. Advantage Insights' Report.

balances that:

- 7.3.1. help improve relationships between retailers and suppliers;
 - 7.3.2. provide assurances that suppliers can speak up safely and have commercial grievances resolved objectively and expeditiously; and
 - 7.3.3. provide a dispute resolution mechanism that is among the strongest in the retail industry anywhere in the world.
- 7.4. For these reasons, we agree with the Commission's preliminary view that any Grocery Code here should, to the greatest extent possible, mirror the provisions of the Australian Grocery Code⁶⁸ (subject to any modifications required to reflect issues unique to the New Zealand retail grocery sector). We consider it a robust and well-considered code (that our parent company Woolworths Group was proud to be a founding signatory of). There would also be significant benefits from a compliance and efficiency perspective for retailers that operate (or intend to operate) on both sides of the Tasman (such as Woolworths, Costco, Aldi, and Metcash) if New Zealand implemented something substantially similar (and presumably benefits for suppliers that operate on both sides of the Tasman too).
- 7.5. While the Australian Grocery Code is voluntary, and we would voluntarily sign-up to a Grocery Code in New Zealand, we believe that any New Zealand Grocery Code should be mandatory. As well as effecting change, a level playing field is also critical. The large number of owner-operated retail grocery stores in New Zealand would mean that a voluntary regime would require a large number of signatories, and significantly heightens the risk of opt-out.
- 7.6. In addition to these considerations, to ensure a mandatory Grocery Code is effective and balanced, we consider that the following would be important features:
- 7.6.1. Applies to all retailers and independent wholesalers: In our view, a mandatory Grocery Code would need to apply to all key participants in the grocery industry – including corporate grocery retailers (such as WWNZ, Costco, and The Warehouse), cooperative grocery coordinators (such as FSNI and FSSI), retail owner-operators (such as individual New World, PAK'nSAVE, Four Square, FreshChoice and SuperValue owners), as well as online retailers, meal-kit suppliers, and independent grocery wholesalers. A principle of broad application would ensure that supplier treatment is consistent across the sector, that all retailers compete on a level playing field, and ensure that the Grocery Code would not constantly need to be revisited. Recognising that this may place a disproportionate compliance burden on very small operators, we suggest there be a minimum size / turnover threshold at which a grocery retailer is not covered (for example, a standalone independent supermarket with no affiliation with a larger supermarket group).
 - 7.6.2. Applies to retailers and suppliers fairly: We consider that key obligations, such as good faith dealing, should also apply to grocery suppliers as well as retailers - especially large multinational grocery suppliers. Reciprocal good faith obligations on both retailers and suppliers would help to:
 - 7.6.2.1. ensure that rights and obligations apply in a consistent way;

⁶⁸ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [9.120].

- 7.6.2.2. ensure that the compliance burden does not fall only on retailers;
 - 7.6.2.3. recognise that creation of a legal / regulatory framework that significantly advantages one side over the other, in bilateral arms'-length commercial negotiations, would have distortionary effects on the commercial negotiation process that may ultimately harm consumers; and
 - 7.6.2.4. recognise that many grocery suppliers are large multinational corporations many times bigger than WWNZ, FSNI, and FSSI, and have higher margins than retailers.
- 7.6.3. Allows for a transition period: To the extent the Grocery Code imposes additional requirements over-and-above existing compliance practices, it will be important that the Grocery Code allows for a sufficient transition period after enactment for all parties to put in place the necessary processes and frameworks to adapt to the new Grocery Code. In our view, that period should be at least 12 months from enactment and apply equally to all parties.
- 7.6.4. Accompanied by guidelines: Our view is that non-binding, and readily accessible, guidelines on the operation of the Grocery Code will also be helpful to facilitate a clear and consistent understanding of their application. Ideally, these would be written with reference to commonplace real-life scenarios from the industry. We would be happy to assist the body responsible for drafting the Grocery Code to prepare these guidelines.
- 7.7. Given the Australian Grocery Code includes specific requirements about the terms that may be included in supply contracts (wastage, shrinkage, promotional funding, variations to contract, quality specifications, labelling / packaging) and obligations to negotiate in good faith, if a similar Grocery Code were introduced in New Zealand (along with the imminent introduction of the prohibitions on unfair contract terms (**UCTs**) in small trade contracts and unconscionable conduct) we would not see any need for a regime to enable suppliers to coordinate together in negotiations with retailers (including as many “non price terms and conditions”⁶⁹ would already be mandated by the Grocery Code).
- 7.8. To the contrary, we consider that there would be a number of potential downsides from allowing such coordination - including:
- 7.8.1. loss of competition - both on price, product quality, and innovation (as the Draft Report notes, supplier coordination could “harm competition. This would include, but not be limited to, cartel conduct”);⁷⁰ and
 - 7.8.2. introduction of additional complexity in contracting and account management - our view is that such a regime would require complex governance and oversight arrangements to manage competing supplier interests in negotiations, including given they could have conflicting interests in terms of product ranging decisions or desires to introduce new products into a category.
- 7.9. For these reasons, we consider that a regime that allowed supplier coordination in bargaining with retailers would risk harm to competition, increased transaction costs, and ultimately

⁶⁹ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [9.130].

⁷⁰ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [9.131.2].

higher prices and less product choice for consumers.

8. We support the introduction of a mandatory unit pricing code

- 8.1. While Countdown already provides unit pricing data for most products that we sell in New Zealand, we acknowledge the concerns raised in the Draft Report about retailers choosing different approaches to the display of unit pricing and we share a desire to make things easy for customers.
- 8.2. Accordingly, we would support the introduction of a mandatory unit pricing code (**Unit Pricing Code**) that aligns with the Australian unit pricing regime. The Australian regime is well understood, and has been considered and adapted to reflect everyday practicalities.
- 8.3. In addition, to ensure a mandatory Unit Pricing Code is effective and balanced, we consider that the following would be important features:
 - 8.3.1. There should be a sufficient transition period for retailers to implement new unit pricing displays across at least a 12 month timeframe, applied equally to all parties. This would allow for necessary system enhancements or reconfiguration to be undertaken (including ticketing systems, and other investment).
 - 8.3.2. Unit pricing requirements should be responsive to technology and other changes (for example, the unique dynamics associated with the increased use of Electronic Shelf Labels (**ESLs**) by retailers, and the importance of creating a regime that caters for new innovations).
 - 8.3.3. Unit pricing requirements should apply to all participants on an equal and uniform basis, including owner-operator competitors and general merchandise retailers that sell grocery items. If unit pricing is limited to only a few select retailers, or is introduced other than in a uniform manner, we see a significant risk of added cost, more confusion for consumers, and distortions in competition. Recognising this may place a disproportionate compliance burden on very small operators, we suggest, like in Australia, there be a minimum floorspace threshold at which a grocery retailer is not covered (for example, standalone grocery retailers with no affiliation with a larger supermarket group and less than 1,000 sqm of floor space not be covered).
 - 8.3.4. Implementation would need to be supported by industry and Government funded awareness programs for consumers to best ensure that the benefits of consumer information and retailer comparison are achieved.

9. We will work with the Commission to further simplify our pricing and promotional practices

- 9.1. We have undertaken a number of initiatives already to simplify our pricing, promotions and Onecard programmes and help consumers make decisions that best meet their needs. Examples include our move towards Everyday Low Pricing (for example, Great Price), our move towards fewer and more meaningful promotions,⁷¹ the recent simplification of our

⁷¹ Countdown's proportion of sales on promotion has decreased from [] in 2014 to []. On this topic, we note that Figure 2.5 of the Draft Report, which relies on data from 2017, is outdated. We made the same point in relation to the same chart and data in our Initial Submission (see our response to question 43). Figure 2.5 of the Draft Report is also inconsistent with the 2019 data in Table E2. It is important that the Commission's Final Report includes up-to-date data, and we request that our updated data on this topic is reflected in the Final Report.

Onecard rewards currency (and improvement in earn rate) in October 2020, and ongoing investment in ESLs (which mitigate the risk of human or ticketing error).

- 9.2. But we agree there is always room for improvement. To this end, we are open to working further with the Commission to discuss ways we (and all retailers) could make pricing and promotional practices clearer still. In this regard, we would welcome the opportunity to work with the Commission to develop clear industry-specific guidelines on promotions and “was / now” pricing so that a fair and consistent approach can be adopted. These guidelines should apply to all competing retailers (for example, pharmacies, green-grocers, liquor stores, Chemist Warehouse, The Warehouse, and online retailers) so that consumers understand and can compare prices and promotions wherever they shop for food and grocery items.
- 9.3. In our view, the guidance to retailers that has been issued by the Commission to date is too high-level to achieve meaningful consistency in practice (for example, “*a ‘usual price’ is the price you commonly sell the goods for*”).⁷² Looking ahead, clear, consistent, and specific retail guidelines could include (amongst other things) guidance or principles that would give direction on:
- 9.3.1. The placement and readability of information on shelf labels and signs (including consideration of ESLs, which are increasingly being implemented in retailers).
 - 9.3.2. The period for which a price needs to have been the “normal” shelf price before it can be used as a reference price for a promotion and how this period differs for different categories of products (for example, fresh produce vs frying pans).
 - 9.3.3. Whether short (1-2 day) sales affect the period a price needs to have been the “normal” shelf price before it can be used as a reference price for a promotion.
 - 9.3.4. Whether offering permanent multibuy savings affects the “normal” shelf price for individual products.
 - 9.3.5. How long a product can be on promotion and whether this is different for different categories of products.
 - 9.3.6. Whether or not retailers can promote “savings” off “recommended retail price” or “estimated retail price”, when that retailer is not itself ordinarily selling at those prices.
 - 9.3.7. When out of season prices can be used as reference prices for seasonal products.
 - 9.3.8. Whether businesses can use a reference price when they have not sold a product at that price before the discount is applied (for example, an introductory special).
 - 9.3.9. How “basket” price comparisons between retailers can be made, and referenced, in advertising. This includes the use of substitute products for comparisons, and how long a basket comparison can be promoted after the actual basket was purchased. This should also recognise that, whilst a basket comparison can be “technically” accurate, because it represents the position at a single point in time, there are a number of factors that can influence that. For example, the date of the relevant shop and any instructions given to the shopper can be highly relevant, and can impact (and misrepresent) the outcome significantly (for example, if the shop is deliberately timed

⁷² Commerce Commission “Price Promotion Tips” (11 May 2017). Retrieved from: https://comcom.govt.nz/_data/assets/pdf_file/0020/64163/Price-promotion-tips-May-2017.pdf

for when a number of higher value items in the basket are on special at one supermarket but not the other, or deliberately scoped to focus on certain items). Other relevant factors include the use of substitute products for comparisons (that is, determining what is a “like-for-like” substitute), and whether the chosen basket reflects that of a typical real-life shopper. We do not consider that the Advertising Standards Authority (**ASA**) guidelines on basket price comparisons are adequate as they oversimplify what is a commonly used, and potentially influential, marketing practice.

- 9.4. In addition, while information about our prices is already readily available to our customers online and in-store, we are also open to exploring with the Commission the provision of regular access or feeds to the retail prices of our packaged goods to enable independent websites to offer freely available price comparison services to consumers (similar to Consumer NZ’s Powerswitch website in the electricity sector). If this option were of interest to the Commission, and supported by other sector participants, we would be open to collaborating on the design principles for how this could be implemented.

10. We will further simplify our Onecard terms and conditions

- 10.1. As part of WWNZ’s commitment to continually improve the Onecard programme, we have recently made a number of changes to ensure consumers are presented with information that makes the programme easier to understand.
- 10.2. However we are keen to improve, and we are open to further change. Such changes could include:
- 10.2.1. Simplifying the format of our Onecard terms and conditions with a “frequently asked questions” style format to more clearly communicate the terms to consumers in an intuitive and digestible form.
 - 10.2.2. Updating our Onecard registration page, along with relevant customer email templates, to include separate links to each of the relevant terms (and links to the new “frequently asked questions” format).
 - 10.2.3. Updating our Privacy Policy, along with how key provisions in those documents are presented, to make them easier for consumers to review and understand. For example, we could look at presenting key provisions through infographics, images or videos to be more engaging and easier to digest than the current, primarily text-based, approach. User experience consumer testing will help shape our final approach.
 - 10.2.4. Making it easier for our customers to understand the types of data that WWNZ collects, including where it is collected from, how it is handled with care, and with whom it is shared (taking a balanced approach to the challenge of ensuring that consumers are sufficiently informed but are not overloaded with information).
- 10.3. We are happy to discuss and consult with the Commission, and to engage with the Privacy Commissioner, as required, to make continued improvements to our Onecard terms and conditions, registration and privacy processes.

11. Establishing a grocery ombudsman or adjudicator

11.1. We recognise that some of the options we have outlined in Part A would require some form of ongoing monitoring and affordable dispute resolution mechanism, for example in relation to the introduction of:

11.1.1. a mandatory Grocery Code;

11.1.2. a mandatory Unit Pricing Code; and

11.1.3. any other initiatives discussed with the Commission in relation to simplifying pricing and promotional practices, simplifying loyalty terms, or facilitating any price comparison website.

11.2. Accordingly, we would be open to supporting specific grocery industry oversight of the new codes / regimes, such as via an ombudsman or adjudicator. This would include legislation providing for a suitable disputes resolution scheme (such as a requirement for a disputes body to be established), as well as legislation including any additional specific functions that need to be covered – for example, monitoring a Unit Pricing Code, and establishing processes for sharing price information with price comparison websites.

Part B: Changes to assist further new entry and expansion

12. Options for assisting further new entry and expansion

- 12.1. Our view is that the sector is already intensely competitive, and is becoming more so, organically, and without intervention.
- 12.2. We are therefore cautious about the more extreme options to assist with new entry and expansion that would be significant and involve internationally unprecedented regulatory intervention (such as forced separations, divestments and regulated access regimes). This is particularly the case given the issues with some of the Draft Report's preliminary findings as set out in Part D.
- 12.3. We recommend the Commission focus on options that:
 - 12.3.1. remove any impediments to further entry or expansion, without undermining the scale and efficiencies of existing grocery retailers; and
 - 12.3.2. best enable the entry and expansion of competitors that are truly independent of (and not reliant on) WWNZ, FSNI, and FSSI's assets or businesses.
- 12.4. The following are measures we think meet this test, subject to careful design and implementation.

13. Law change to make exclusive leases and land covenants / encumbrances unenforceable

- 13.1. While we consider there are legitimate and pro-competitive reasons for exclusivity provisions in WWNZ's leases with landlords and restrictive land covenants (that is, to underpin investment in new supermarkets and protect goodwill),⁷³ we note the Draft Report's preliminary view that "restrictive covenants and exclusivity covenants in leases on sites that might otherwise be suitable for retail grocery development... is likely to be a significant factor preventing or slowing entry and expansion."⁷⁴
- 13.2. To remove that potential impediment to new entry or expansion, we would support a regime that, generally:
 - 13.2.1. makes such lease provisions unenforceable in the New Zealand retail grocery sector after a certain period following investment in a new site (say, 5 years); and

⁷³ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [6.86] and [6.87].

⁷⁴ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [6.73].

- 13.2.2. makes such covenants unenforceable in the New Zealand retail grocery sector after a certain period following investment in a new site (again, say, 5 years).⁷⁵
- 13.3. This would, in effect, mirror the position in Australia where such lease provisions are unenforceable (due to voluntary undertakings to the ACCC),⁷⁶ but would expand on that by also applying to covenants, whilst allowing the application of such provisions and covenants for five years following investment in new developments (both for future new developments, and new developments that have been completed in the last 5 years), or where necessary for the operation of a supermarket on a particular site. While we believe our use of such provisions and covenants has been to protect legitimate investments and interests (and we are not aware of them causing issues for any new entrants), we are conscious of the Commission's desire to remove any potential impediments to new entry, and we note that the ACCC considers that the equivalent undertakings in Australia have made a meaningful change:
- 13.3.1. The ACCC has noted that "[t]he undertakings have led to an increase in the number of shopping centres with more than one supermarket, thus creating more competition and leading to lower prices for consumers than in shopping centres with only one supermarket".⁷⁷
- 13.3.2. Since the undertakings were given Aldi has grown in Australia from 170 stores (at the time of the ACCC's market study in 2008)⁷⁸ to 590 this year.⁷⁹
- 13.4. Such a law change would need to be limited to lease provisions / covenants solely directed at preventing a competing supermarket, and it would be important (as noted at paragraph 9.92 of the Draft Report) that it does not apply to other lease provisions / covenants directed at other terms that are necessary to operate a supermarket (for example, terms requiring the provision of facilities and amenities such as car parks, trolley bays, access, sight lines, signage or terms allowing rental abatements or offsets in response to failures by the lessor to

⁷⁵ Our view is that a 5 year period of enforceability following investment in a new site is the minimum necessary to enable continued investment in new supermarkets. This is because for a new supermarket it is WWNZ that invests in the fitout and development of the premises. However, in the case of a leased premise in a shopping centre, it is the landlord that has control over how the commercial environment in the shopping centre can change (for example, by changing the mix of other tenants and not investing the shopping centre amenities). So the landlord has control over those important matters, but it is the tenant that will bear the commercial consequences of that. For example, if WWNZ is considering investment in the fitout and development of a new supermarket, but the landlord is retaining discretion over changes to the tenancy mix of the shopping centre from day one, then WWNZ will not have the same commercial certainty on its operating environment to justify the investment in the fitout and development of the site that it otherwise could. The same equally holds true where, instead of leasing a site, WWNZ is purchasing land for a new supermarket. In those circumstances WWNZ will not have a lease to protect its commercial environment, but where the seller of that land is retaining adjoining property, WWNZ and the seller can agree a covenant on that adjoining land for a short period of time to provide the necessary commercial certainty on WWNZ's operating environment so that it can make the necessary investments. In many of these instances, we consider that periods longer than 5 years would, in fact, be necessary to adequately protect investments, but we are content to support a regime with a 5 year maximum (both for future new developments, and new developments that have been completed in the last 5 years).

⁷⁶ Due to undertakings given by each of Woolworths, Coles, Supabar, Aldi, Franklins, SPAR, Foodworks, and Metcash. See: <https://www.accc.gov.au/media-release/phase-out-of-supermarket-restrictive-lease-provisions-supabarn-undertaking>

⁷⁷ Commitment Decisions in Antitrust Cases. Note by Australia. 15 – 17 June 2016.

⁷⁸ ACCC, "Report of the ACCC inquiry into the competitiveness of retail prices for standard groceries (July 2008) at [3.3.1].

⁷⁹ (21 March 2021) Aldi eyes smaller stores, e-commerce as sales reach \$10.5b. Financial Review. See: <https://www.afr.com/companies/retail/aldi-eyes-smaller-stores-e-commerce-as-sales-reach-10-5b-20210318-p57by3>

provide services or undertake maintenance).

- 13.5. We consider this would require a law change, rather than voluntary undertakings from WWNZ, FSSI, and FSNI:

13.5.1. For the reasons outlined in paragraph 9.90.1 of the Draft Report that there can be difficulties with removing existing covenants and encumbrances registered or noted on title to land.

13.5.2. In respect of FSSI and FSNI, it is often the case that covenants or leases are in the name of individual store owners, or related parties (rather than FSNI or FSSI themselves), and so a voluntary regime would require separate undertakings from a large number of different parties.

- 13.6. Such law change should also make unenforceable any lease provisions that prevent a lessee from opening or operating a new supermarket within a prescribed area,⁸⁰ again after a certain period following investment in a new site by a landlord (say, 5 years).

14. Law change to restrict exclusivity provisions in standard supply contracts with grocery suppliers

14.1. While WWNZ does not have many exclusive supply contracts with grocery suppliers, we note the comments in the Draft Report that such contracts “may potentially impact on entry and expansion”.⁸¹ We would, therefore, support a regime that makes exclusivity provisions unenforceable in the New Zealand retail grocery sector except where they are reasonably necessary for legitimate business purposes, such as where they have been included in integrated (non-standard) supply relationships.

14.2. We consider that this exception for provisions that are “reasonably necessary” (a concept used in a number of other legal contexts) for legitimate business purposes is required to ensure that such a regime does not undermine the ability of retailers and suppliers / manufacturers to partner together on co-investments for mutual benefit and / or the benefit of consumers. That could include where a retailer and manufacturer partner together to underpin investment in a new manufacturing site (for example, WWNZ’s partnership with Hilton Foods to establish a new meat processing plant), or where a retailer and supplier partner together in developing a new product or brand (for example, WWNZ working with suppliers to transition to organic sourcing and production to expand WWNZ’s organic offering) or co-investments in intellectual property.

15. Law change to make “best price” clauses unenforceable

15.1. While WWNZ does not actively monitor or enforce any “best price” clauses,⁸² and we no longer include such clauses in our standard terms, we note the comments in the Draft Report that such contracts “may potentially impact on entry and expansion”.⁸³ We would, therefore, support a regime that makes such best price clauses unenforceable in the New Zealand retail grocery sector.

⁸⁰ Known as “trading radius” clauses.

⁸¹ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [6.170].

⁸² Sometimes called “most favoured nation” or “MFN” clauses.

⁸³ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [6.170].

16. Law change to New Zealand's planning regulations to assist in entry and development of new retail grocery sites

- 16.1. We agree with the Draft Report's findings that New Zealand's planning regulations, including the RMA (together **Planning Regulations**), often impose unnecessarily lengthy and costly impediments to the development of new supermarkets in New Zealand. In our view, those Planning Regulations are the primary impediment to the development of new supermarkets (and to be clear - that is not because retailers oppose their competitors' resource consent applications for anti-competitive reasons⁸⁴ - that has been outlawed since 2009).
- 16.2. Rather, amongst other reasons, it is because councils are reluctant to enable surplus developable land for supermarkets and restrict the locations where supermarkets can be developed (by focussing on "centres" and through overly restrictive policies to prevent non-retail zoned land to be rezoned for retailing), and District Plans contain onerous or impractical controls in relation to supermarkets (or areas in which a supermarket may be located).
- 16.3. Therefore, we would support changes to New Zealand's Planning Regulations to assist in the entry and development of new retail grocery sites, including:
 - 16.3.1. The inclusion of directive outcomes regarding commercial land supply (in addition to housing supply). This should include recognition of the inherent links and relationship between essential commercial / retail activities like grocery supply or supermarkets to the development of new housing supply.
 - 16.3.2. Requirements on councils to take a more enabling approach to activities such as supermarkets within the planning documents, including a more enabling approach to applications to rezone land for retail purposes.
 - 16.3.3. Improving the efficiency of the consenting process for urban developments, such as supermarkets.
 - 16.3.4. Greater recognition of the positive benefits of development. This could include recognition of:
 - 16.3.4.1. The essential service provided by supermarkets, as heightened by the experience during COVID-19.
 - 16.3.4.2. The benefits of additional competition in the market.⁸⁵
 - 16.3.5. Retention of the trade competition provisions in the RMA, which restrict opposition to consents for anti-competitive reasons. This would continue the effective regime currently in place, since 2009.

⁸⁴ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [6.104.02].

⁸⁵ As discussed in paragraph 6.114 of the Draft Report.

17. Law changes to the Overseas Investment Act to lower the regulatory impediments to entry / expansion by “overseas” supermarket operators such as Costco and Aldi

- 17.1. Our view is that it would be beneficial for the OIA to be amended to level the playing field between domestic and overseas retailers.
- 17.2. Specifically, “overseas persons” (as defined in the OIA), which would include Costco, Aldi, and WWNZ, must apply to the Overseas Investment Office (**OIO**) on each occasion that they wish to purchase or lease “sensitive land” for a new store. This would most likely be required when they are seeking to develop new distribution facilities in non-urban areas, or when acquiring residential land to build a new store or extend an existing store.
- 17.3. Amending this regime would lower the impediments to new entry and expansion by such “overseas” retailers. In particular, the requirement to obtain OIO consent:
- 17.3.1. Inevitably impedes the speed that an “overseas” owned retailer can open new and improved stores or, in some cases, establish or extend its distribution network. The consenting process (particularly for sensitive land) takes a number of months.
- 17.3.2. Can place “overseas” owned retailers at a competitive disadvantage in acquiring sites where there is competition for the land from “non-overseas persons” (which FSNI, FSSI, and their cooperative members would be). In the worst case, this can lead to lost opportunities where vendors or developers prefer to contract with a “non-overseas” purchaser because of the additional risks and delays involved in transacting with an “overseas” person.⁸⁶
- 17.3.3. Is expensive:
- 17.3.3.1. For consent to acquire residential land, an “overseas” supermarket operator would incur a fee of \$225,000 (plus GST) for a standing consent to acquire 10 residential properties (and that excludes costs involved in preparing an application).
- 17.3.3.2. For consent to acquire sensitive land which is not residential, an “overseas” supermarket operator would incur a fee between \$68,000 and \$146,000 (plus GST) (again, that excludes costs involved in preparing an application).
- 17.4. Recent changes to the OIA have gone a long way to remove lower-risk transactions from requiring consent and to simplify investor requirements (and the standing consent regime for residential land can help smooth the path). However, it would be helpful to further level the playing field between “overseas” and “non-overseas” persons by allowing retailers to obtain general class-based exemptions for the development of grocery stores or distribution centres, or to allow for longer periods on standing consents for residential land, rather than needing to apply to the OIO for each and every specific land interest where sensitive land may be involved or, where residential land is involved, obtain speculative standing consents every 2 to 3 years.

⁸⁶ Where there is competition for the land from “non-overseas persons”, those “non-overseas persons” can offer greater certainty of the project progressing, and enable the vendor or developer to benefit from lower holding costs for the land, less risk of construction cost inflation, and greater speed to achieve return on investment.

18. Assisting (or authorising) the formation of joint buying groups by independent retailers

- 18.1. A key premise underpinning the wholesale options canvassed in the Draft Report is that “other grocery retailers that offer a main shop have consistently indicated that they largely receive less competitive prices than the major grocery retailers when purchasing from suppliers directly due to differences in volume.”⁸⁷ To the extent this is a key concern of the Commission, we suggest the Commission consider options to facilitate independent retailers to engage in joint buying groups.
- 18.2. That joint buying groups can enhance competition and facilitate new or expansion is reflected in:
 - 18.2.1. the fact that FSNI and FSSI themselves began as joint buying groups of independent retailers, and have grown from there;⁸⁸ and
 - 18.2.2. the express exemption of “collective acquisitions” among competing firms from the Australian cartel rules,⁸⁹ and the authorisations granted by the ACCC in Australia to facilitate independent supermarkets to collectively negotiate with grocery suppliers.⁹⁰ For example, the ACCC has noted that allowing collective bargaining would “effectively [allow the buying group] to act as a new wholesale level competitor”, “achieve transaction and logistic costs savings”, “increase efficiency in delivery arrangements and materially lower distribution charges”, “introduce new competitive pressure on existing acquirers of goods and grocery products” and “allow the independent supermarkets to improve their offerings to consumers (including through lower retail prices), and enable them to compete with their retail competitors more effectively.”⁹¹
- 18.3. To the extent the Commission considers that the ability to negotiate volume discounts with suppliers is an impediment to the growth of independent retailers, the Commission could similarly consider authorising the formation of joint buying groups by independent retailers, or suggest a law change to provide a class-based statutory exception for joint buying by independent retailers.
- 18.4. The Commission could also give consideration to suggesting amendments to the existing joint buying exception in the Commerce Act given in August 2017 the exception became narrower than the cartel prohibition it provides protection from (as the joint buying exception only provides an exception to price-fixing, not the expanded categories of prohibited conduct). It is recognised that this change has made the business community more reluctant to rely on the

⁸⁷ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [6.130].

⁸⁸ “We’ve been serving New Zealanders since 1922, when a young lad named J. Heaton Barker called together members of the Auckland Masters Grocers Association to discuss plans for the formation of a Co-operative (Co-op) buying group”. See: <https://www.foodstuffs.co.nz/who-we-are/our-story>

⁸⁹ See s 45AU of the Australian *Competition and Consumer Act* 2010.

⁹⁰ ACCC Final Determination, “collective bargaining with suppliers of goods and services to the Australian grocery industry” (7 April 2020). Available at: https://www.accc.gov.au/system/files/public-registers/documents/Final%20Determination%20-%2007.04.20%20-%20PR%20-%20AA1000457%20Supermarket%20Co-op_1.pdf

⁹¹ ACCC Final Determination, “collective bargaining with suppliers of goods and services to the Australian grocery industry” (7 April 2020) at [4.18].

“joint buying” exception than they were prior to August 2017.⁹²

⁹² This has been noted in recent submissions to the Economic Development, Science and Innovation Committee: “This has resulted in businesses refusing to enter into pro-competitive and efficiency enhancing buying groups as the exception does not provide sufficient protection. This issue has been further exacerbated now that cartel conduct has been criminalised.” Russell McVeagh (30 April 2021) Submission to the Economic Development, Science and Innovation Committee. Commerce Amendment Bill 2021. Available at: https://www.parliament.nz/resource/en-NZ/53SCED_EVI_108304_ED570/6038fd0de25bec0f92940b4b27839e406112294e

Part C: We have an open mind to negotiating wholesale supply contracts, but we believe significant regulatory interventions would not be in Kiwis' best interests

19. Regulatory interventions would be costly and risky

- 19.1. New Zealand's grocery retail sector is already competitive, and is becoming more so, organically, and without intervention.
- 19.2. The Commission is not dealing in this Market Study with a case of "market failure" or a natural monopoly (or state-owned) infrastructure asset. Retail grocery food prices have decreased in real terms over the last decade and customer satisfaction has measurably increased.⁹³ We also disagree that the sector is making excess returns, that retail prices in New Zealand are high, and that there is a lack of competition (see Part D for further details).
- 19.3. We, therefore, do not consider there is any case for significant and internationally unprecedented regulatory intervention (forced separations, divestments, regulated access regimes etc). Beyond the fact that these options would be unnecessary and counterproductive, and that they would be based on questionable findings, they are also at odds with a modern, deregulated and open economy.
- 19.4. On any view, such unprecedented regulatory intervention should only be a "last resort". Such intervention should definitely not be seriously proposed or adopted until other regulatory changes as discussed above, have been implemented, given time to change behaviours, and their impact and effectiveness carefully reviewed, including in a market that continues to quickly evolve (for example, online grocery retailing).
- 19.5. The Draft Report acknowledges that it has not examined "the wholesale level in great detail",⁹⁴ that no cost / benefit analysis had been conducted on these options, and that they carry significant risk of "lost efficiencies", "costs", and "distortion of investment incentives" (including beyond the grocery market).⁹⁵ We agree. Our view is such interventions would:
- 19.5.1. undermine efficiencies (particularly problematic for New Zealand given we are already a very small market);
 - 19.5.2. undermine incentives to invest - both in the New Zealand grocery sector, and the broader economy;
 - 19.5.3. risk market distortion (for example, would Costco, the world's second-largest "bricks-and-mortar" retailer, also be subject to regulation, or just WWNZ, FSNI, and FSSI?);

⁹³ Customer satisfaction with our Countdown offering is increasing over time (reflected in significant increases in our 'Net Promoter' and 'Voice of Customer' scores), as set out in WWNZ's Submission on the Preliminary Issues Paper.

⁹⁴ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [6.144].

⁹⁵ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [9.64].

- 19.5.4. create significant costs - in regulatory design, implementation, and ongoing monitoring. Globally there is no precedent of any intervention in, or economic regulation of, grocery markets of this nature. This means there would be significant design costs in developing any regime, and significant ongoing monitoring and administration costs in trying to monitor outcomes in a market with multitudes of competitors operating differentiated business models to compete across thousands of products;
- 19.5.5. re-allocate assets / value to questionable ends - for example, how could a third player reliant on existing competitors' assets or supply chains through a regulatory framework be said to be a true independent competitor? Or how could one constructed from an arbitrary combination of divested assets be expected to efficiently compete?; and
- 19.5.6. likely (given everything above) ultimately lead to higher prices and poorer outcomes for consumers.

19.6. It is critical the Commission understands these risks. In this Part C, we elaborate further.

20. The reasons why supermarkets are vertically integrated

- 20.1. The Commission has said vertical separation (either operational or structural) of WWNZ, FSNI, and / or FSSI is one of the options it is considering. This would be counterproductive for New Zealand and "regulatory takings" of this nature are not something that should be done lightly (see further at paragraph 21.2 below).⁹⁶ Vertical separation would add cost, risk and introduce inefficiency ultimately costing consumers at the check-out.
- 20.2. Vertically integrated supply chains are structured for efficiency⁹⁷ and the ability to innovate. Efficiency comes from greater economies of scale and scope, and the avoidance of layers in the supply chain where each charges a margin to the next (that is, avoids "double-marginalisation"). Efficiency derives also from the flow of information within one entity - the ability to manage complexity, risk, ensuring reliability and control over the provenance and traceability of products, and ensuring appropriate product allocation - especially with peaks and troughs in demand, and unexpected shocks to either supply or demand - for example, product shortages, or COVID-19 purchasing patterns.
- 20.3. The COVID-19 environment is a good example of the benefits of an integrated supply chain. Faced with unprecedented demand spikes, WWNZ has consistently been able to use its integrated model to effectively deploy an "all of system" response to meet Kiwis' needs in a time of crisis. This includes: smoothing extreme demand through the imposition of purchase limits on certain products (and, in the case of a two week period around the time of the first COVID-19 lockdown, temporary changes to Countdown's promotional programme in order to try to manage the impact of "panic buying"); centrally optimising the allocation of product to stores (for example, prioritising remote communities); optimising replenishment through adjustments to store opening hours (to allow more time to replenish shelves) and adjusting order volumes so as not to overload picking capacity; applying uplift adjustments to orders for

⁹⁶ "Moreover, while on the micro level, a state deprivation of property rights by regulation might not appear to engage the question of the integrity of democracy, a general degradation of rights in property across society can undermine the independence and self-reliance aspects of private property that are important for a sound democracy." See: (5 October 2018) Patrick O'Boyle, "Expanding the Constitutional Protection of Property Rights to Address Regulatory Takings."

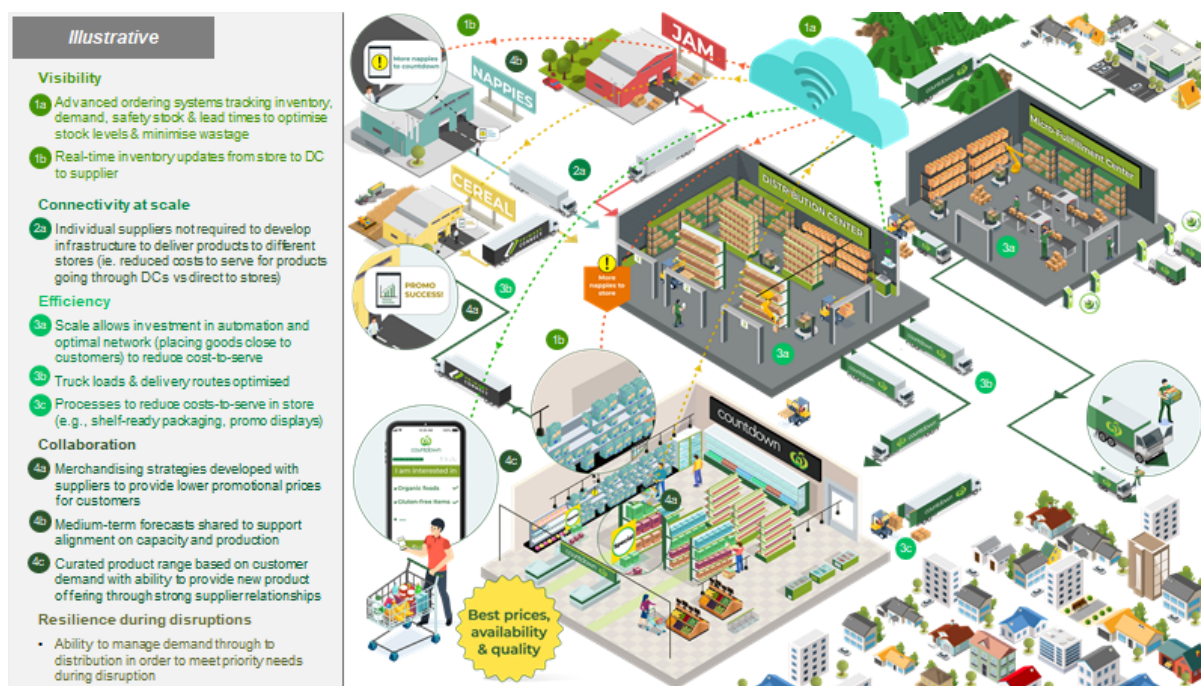
⁹⁷ This was recognised in the Draft Report (at [6.115.1]), where it stated that major grocery retailers "generate cost efficiencies through vertically integrated wholesale and distribution".

key COVID-19 impacted lines; partnering with suppliers to shift certain lines into direct-to-store deliveries (so as to free up DC capacity) and more. The benefits of vertical integration in this ongoing crisis response are well recognised:⁹⁸

“Almost all businesses with some degree of vertical integration did much better [in response to COVID-19] than those without. Coincidence? Probably not. Vertically-integrated companies are structurally better-adapted to handle adverse conditions.... vertically integrated businesses have a greater capacity for agility and are more able to adjust the entire supply process to accommodate a sudden change in demand. These businesses have had the added advantage of limiting losses via a diminished stock risk.”

20.4. How an integrated supply chain works in practice is illustrated in Exhibit C1 below.

Exhibit C1: Benefits of vertical integration resulting in smooth flow of goods across the value chain and lower costs-to-serve



20.5. It is no coincidence that the major supermarket chains across the OECD are also vertically integrated - for example, Tesco, Sainsbury's, Asda, Coop and Morrisons in the UK, Coles, Woolworths, Costco and Aldi in Australia, and other major international retailers including Kroger, Walmart, Carrefour, Mercadona and Lidl.

20.6. By contrast, Metcash's lack of vertical integration has been identified by analysts in Australia as a cause of inefficiency, underinvestment in supply chain, and declining market share:⁹⁹

⁹⁸ The Strain of COVID on retailers - How vertical integration gives companies resilience. Retailisation. Retrieved from: <https://retailisation.com/how-vertical-integration-gives-companies-resilience/>

⁹⁹ (16 January 2020). Metcash urged to sell food arm as majors ramp up investment. The Sydney Morning Herald. Statement made by Credit Suisse analyst Grant Saligari.

“The issue that Metcash faces is reflected in more than a decade of declining market share, it’s not a new issue. This misalignment of ownership is a significant impediment to Metcash putting the appropriate level of investment into areas such as warehouse automation and data analytics. This can significantly improve your range and stock availability, but a lot of those benefits accrue only to the retailer. So it’s difficult for Metcash to make those investments because it doesn’t actually capture the benefits.”

20.7. Reflecting this, in 2019 Metcash’s largest wholesale customer, Drake’s, ceased buying via Metcash, instead choosing to vertically integrate by establishing its own distribution centre and forming direct relationships with suppliers. In doing so, Drake’s managing director said “[w]e know we need to be more competitive; the market is changing. We believe that we’ve got to be vertically integrated... for us to remain competitive, to be able to give our consumer the right goods at the right price, then we’ve got to just strip costs out of the business.”¹⁰⁰

20.8. In sum, the benefits of vertical integration are real, significant and not to be risked lightly.

20.9. Given the stakes and the probability of unintended consequences, robust cost / benefit analysis would need to be undertaken before giving serious thought to vertical separation as an option.

21. Forcing divestments would undermine efficiencies

21.1. Another option raised was the forced divestment by the major grocery retailers of existing assets (for example, stores, brands, or other assets) to create an additional market participant.

21.2. Again, we are skeptical as to how this would result in net consumer benefit. First, it seems unlikely that an arbitrary combination of divested assets would be in a position to efficiently compete. Second, and more importantly, achieving this would obviously come at enormous cost:

21.2.1. As noted at paragraph 20.1 above, “regulatory takings” are not something that should be done lightly.¹⁰¹ It is recognised that it is important that “people have the confidence to invest in property in ways that yield productive returns and growth to support the economic needs of a modern society.”¹⁰² Such steps would be unparalleled internationally, and could have implications for New Zealand’s standing as a place to do business and invest. As the Draft Report notes,¹⁰³ the risks to investment would extend beyond grocery out into the broader economy.¹⁰⁴

¹⁰⁰ (26 September 2019). Drakes departs Metcash to go solo with opening of \$125m DC. Inside FMCG. Retrieved from:

<https://insidemcgc.com.au/2019/09/26/drakes-departs-metcash-to-go-solo-with-opening-of-125m-dc/>

¹⁰¹ (5 October 2018) Patrick O’Boyle, “Expanding the Constitutional Protection of Property Rights to Address Regulatory Takings.”

¹⁰² (5 October 2018) Patrick O’Boyle, “Expanding the Constitutional Protection of Property Rights to Address Regulatory Takings.”

¹⁰³ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [9.64].

¹⁰⁴ “Economists largely agree that empirical evidence demonstrates that nations with strong institutional protection of property rights is important for economic performance by ensuring resources are efficiently allocated”. As quoted in (5 October 2018) Patrick O’Boyle, “Expanding the Constitutional Protection of Property Rights to Address Regulatory Takings” at page 15, which references (2007) Mark Gradstein, “Inequality, Democracy and the Protection of Property Rights” 117 The Economic Journal 252 at [252]. Moreover, O’Boyle notes that, “If security and confidence in property rights is undermined by weak protection of property rights, this is likely to cause underinvestment and thus sub-optimal societal Welfare” (see page 18).

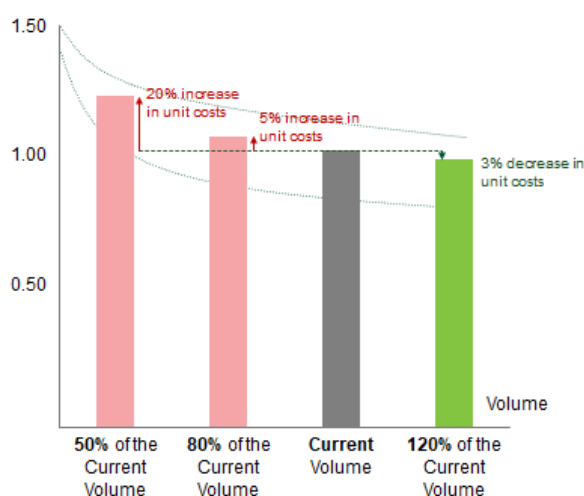
- 21.2.2. Forced divestments would also undermine the economies of scale in our business.¹⁰⁵ We are already a small supermarket retailer by global standards - serving a market with a smaller population than Sydney, but spread across a long, skinny island chain separated by a body of water.¹⁰⁶ Any steps that undermine scale would increase costs significantly, undermine the ability to invest further and flow through to consumers as higher prices - see Exhibit C2 below.

Exhibit C2: Illustrative impact of scale on costs-to-serve¹⁰⁷

Impact of scale on costs-to-serve

Illustrative

Unit Cost normalised index



Typical drivers of unit cost reduction:



The ability to spread multiple fixed costs (associated with employee costs, utility costs, supply chain assets, marketing, IT costs, etc) over greater volumes



Reduced losses in stores due to higher throughput



Higher truck utilisation and route optimisation from higher volume deliveries and higher density of destination stores respectively

- 21.2.3. We also question the relevance of the Draft Report's reference to the Commission's divestment regime in its Mergers and Acquisition Guidelines.¹⁰⁸ These guidelines refer to voluntary divestments in the context of a merger, and assess whether a divested business will be viable. That is not the option floated here. Here, the subject matter is potential forced divestments on existing businesses, and so the key focus should be on what impacts that divestment would have on the ongoing operational efficiency of the party forced to make the divestment.

22. A regulated access regime would be complicated, costly, and most likely unworkable

- 22.1. Another of the options canvassed by the Commission was a regulated wholesale access regime. The Draft Report correctly identifies the significant challenge of trying to impose a regulated access model in an industry with the complexity of grocery. The Draft Report notes that the large number of products would mean regulation would "likely be costly and difficult"¹⁰⁹ and, therefore, ruled out price or returns regulation.

¹⁰⁵ The Draft Report noted at [6.115.2]) that the major grocery retailers are able to "access economies of scale by spreading their fixed costs across large volumes or number of stores, achieving lower cost per unit".

¹⁰⁶ The Draft Report noted the significant risk of "lost efficiencies resulting from the loss of vertical integration caused by separation" at [9.64].

¹⁰⁷ Source: illustrative extrapolation informed by Countdown financials.

¹⁰⁸ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [9.59].

¹⁰⁹ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [9.50].

- 22.2. We agree that such a regime would be costly and difficult. Even without price or returns regulation, implementing an access regime for wholesale groceries would be fraught with difficulty.
- 22.3. Grocery wholesaling is also not the *type* of industry ordinarily regarded as potentially amenable to such intervention. Wholesale access regimes are usually only considered where:
- 22.3.1. there is a “natural monopoly” asset (such as a telecommunications, electricity or gas distribution network, a rail track or network, or a port - often current or former statutory monopolies);
 - 22.3.2. that “natural monopoly” is an essential or a non-substitutable input into further production for downstream competition (that is, an “enduring bottleneck”) - in other words, there is no alternative input or process that enables a competitor to produce an equivalent final good or service;
 - 22.3.3. the costs of production by the “natural monopoly” involve large fixed (infrastructure) costs and comparatively low (ongoing) variable costs;
 - 22.3.4. the “natural monopoly's” investments are largely sunk in long-running stable infrastructure assets (rather than being a dynamic and innovative industry, with constant new investments); and
 - 22.3.5. that “natural monopoly” supplies one (or very few) undifferentiated product(s) (such as the use of a power cable or a rail network by an electricity supplier or rail services operator respectively), such that the design, implementation, and monitoring of any access regime can be manageable.
- 22.4. Even at a stretch, none of these criteria are met in the case of grocery. See Exhibit C3 below for further illustration.

Exhibit C3: Illustrative characteristics of industries where access is typically regulated

Characteristics that define industries where access is typically regulated globally						Illustrative	
	 Communications (telco, internet)	 Energy (gas, electricity)	 Transport (rail, ports)	 Wholesale access to fuel	 Wholesale access to grocery retail	Comments (on grocery retail)	Conclusions
Extent of natural monopoly (where duplicating infrastructure would not be in customers' interests due to high sunk costs)	High	High	High	Medium	Low	• Not as capital-intensive, more variable costs and possible to duplicate cost-effectively.	The wholesale grocery retail sector does not meet the need for wholesale access regulation
Limited/no other alternative for access to market by retail competitors	High	High	High	High	Medium	• New market entrants do not need incumbents as only way to source product	
Complete control over asset and resulting pricing	High	High	High	Medium	Low	• Grocery wholesaler does not have full control over access to supply or pricing	
Non-substitutability of end-product	Medium	High	High	High	Low	• There is substitutability in grocery retail (e.g., via other stores, restaurants, takeaway food, online etc.)	The wholesale grocery retail market is far more complex to regulate than other typically regulated markets
Homogenous product(s) with minimal/no changes to offering over time	Medium	High	High	High	Low	• Thousands of differentiated SKUs, non-product / non-price values important to customer, ever-changing preferences	
Ease of participation in access regime (e.g., plug and play)	High	High	High	High	Low	• Requires catered service offering for different wholesale customers; no "one-size-fits-all"	

22.5. For these reasons, we are clear that any regime that seeks to regulate wholesale supply, either through access undertakings or regulations, would be unworkably complex, costly, and create significant risk of unintended consequences, loss of innovation and investment, and ultimately higher grocery prices for consumers. Specifically, we raise the following points for the Commission to consider:

22.5.1. Globally there is no precedent or experience of ex-ante economic regulation of grocery wholesale markets. This means no precedent to work from, significant design costs to develop a regime that is "fit for purpose", and large risk of "unknown unknowns" - extremely challenging to regulate for, and likely costly to administer.

22.5.2. WWNZ does not have supply terms (or prices) for its internal supply chain. Countdown stores are not charged an internal 'price' for their supply, and while SuperValue and FreshChoice outlets are owner-operated, these are franchises (with all the mutual obligations, including terms of supply, that come with that) - which is different from an arms-length wholesale customer. In other words, there is no existing ready-made benchmark or comparator with which to point to and identify "non-discriminatory" terms.

22.5.3. This is not a sector like telecommunications or electricity networks, where a mobile telephony provider, or an electricity retailer, can "plug and play" into existing infrastructure service. In groceries, every wholesale customer would have different requirements - see Exhibit C7 below - and there would be benefits to accommodating flexibility rather than trying to design a "one-size-fits-all". Therefore, there would be a range of bespoke matters that would need to be agreed between a wholesaler and wholesale customer in any given relationship. Those are matters that could be agreed through bilateral commercial negotiations (where risk, reward, and costs are appropriately balanced and agreed). However, given those multitudes of different requirements, trying to determine, regulate, and monitor what is "non-discriminatory" between different wholesale customers would be extraordinarily difficult. For

example:

- 22.5.3.1. A wholesale customer that wishes to order from WWNZ through an integration of systems to enable automatic ordering (including automated demand and replenishment planning) would have a lower cost to serve than a wholesale customer that wishes to order on an ad hoc basis.
- 22.5.3.2. A wholesale customer that wants wholesale supply of 10,000 of our SKUs would have a different cost to serve than a customer that wants just 100 SKUs.
- 22.5.3.3. A wholesale customer that wants packaged products only would have a different cost to serve to a customer that wants a mix of fresh and packaged products.
- 22.5.3.4. A wholesale customer that wants to pick up products from WWNZ's DC would have a different cost to serve than a customer that wants delivery to a network of their own stores (or delivery to their own DC).
- 22.5.3.5. A wholesale customer that wants delivery to locations closer to our existing network (locations of our stores and DCs) would have a different cost to serve than a wholesale customer with a different geographic profile.

22.5.4. For these reasons:

- 22.5.4.1. Determining what are "non-discriminatory" terms and conditions of supply would be extraordinarily difficult given the multitude and complexity of different customer needs (which would no doubt differ from WWNZ's own retail demand). While "non-discriminatory" is a fine concept in principle, there would be significant difficulties in trying to translate this into clear-cut commercial terms. To cover off the range of potential scenarios, and that each different wholesale customer would have different requirements, any access undertaking or regulation would likely run into hundreds, if not thousands of pages, and even then get things wrong.
- 22.5.4.2. Monitoring the terms and conditions of access would be a significant and ongoing task - and the costs and efforts involved in seeking to monitor non-discrimination would likely be significant.
- 22.5.4.3. Resolving inevitable disputes about access and pricing in this context would be unworkable. Even where there is just a single infrastructure service, resolving disputes on access terms or "non-discriminatory" pricing issues often takes many years.¹¹⁰

22.5.5. The "incumbent firms'" assets have been invested in, and developed, through a process of innovation in competitive markets. That is a different scenario to contemplating access regulation on former statutory monopolies. This raises some additional key questions:

¹¹⁰ See for example, the Queensland Competition Authority's experience in reviewing and approving rail and port services access undertakings, over many years.

- 22.5.5.1. WWNZ's supply chain is already at capacity at certain points of the year (for example, Christmas, Easter, COVID-19 demand shocks). Who would pay for the investment to expand capacity to enable regulated wholesale access? Would regulations mandate that investment? If so, who would determine what is an appropriate level of capacity and whether any investment is efficient?
- 22.5.5.2. How would such a regime be designed to incentivise continued investment and reward innovation by incumbent firms? See Part D below for further discussion on innovation and investment.
- 22.5.5.3. How would the regime be designed to avoid disincentivising new entrants from investing in their own new innovation and supply chains? Again, see Part D below.
- 22.5.5.4. Assuming dynamic competition and innovation continues (despite the risks that regulated access might pose to that), how would the access regime be designed if what is "best practice" wholesale supply is a "moving target" (due to that continued dynamism)?
- 22.5.5.5. How would the regime avoid putting the "incumbent firms" at a competitive disadvantage (due to over-regulation), when faced with the inevitable expansion and competition from Costco, Aldi, and others?
- 22.5.5.6. Will new entrants that invest in their own supply chain (for example, Costco and Aldi) also be subject to a regulated access regime? Would that possibility materially reduce their incentives to enter or expand in New Zealand, or under-invest?
- 22.5.5.7. Given those businesses (Costco and Aldi) are many times larger than Woolworths internationally, could WWNZ become an access seeker to benefit from their investments?

22.5.6. As noted in the Draft Report, there could also be significant risks for New Zealand's standing as a place to invest and do business (not just in groceries, but across all sectors),¹¹¹ if wholesale access regulations were implemented in an industry such as this, in particular where such intervention is not supported by robust findings of a competition issue.

22.6. In summary, our view is that raising this as a potential option significantly underestimates the challenges that the Commission would face in designing, implementing and enforcing effective access remedies, and that such a step would, in our view, be practically unworkable, disincentivise investment, and ultimately lead to higher prices to consumers.

23. Significant and novel regulation (such as an access regime, forced separation, or forced divestments) will prevent new investment in the sector, and prevent dynamic competition on innovation

23.1. Our industry is more than just warehouses, trucks, and supermarkets. We need to ensure we can get goods to where our customers want them - at the right time, in the right quantities,

¹¹¹ As noted at paragraph 9.64 of the Draft Report in relation to vertical separation, but the same would equally apply in relation to mandated wholesale access.

and at the right temperature and quality and to meet a range of changing customer needs (see section 20 above). This requires continued investment in our end-to-end supply chain (including partnering with third-party logistics providers) to ensure it is efficient, flexible and resilient to shocks.

- 23.2. Increasingly, new technologies and innovations are emerging to help make this happen. Artificial intelligence (**AI**), machine learning and computer vision, picking, sorting and sensor technologies, automated distribution centres, dark stores, automated micro-fulfillment centers, drop-shipping from manufacturers, route optimisation analytics, temperature-controlled facilities, just in time delivery, hardware like drones, robots, automated guided vehicles, and autonomous vehicles are but a few of these innovations. These technologies can be used to streamline distribution and optimise pallet packing, truck loading, and delivery routes to enable the most efficient unloading and product handling at the other end. New technology is also driving improved environmental and safety outcomes (for example, safety sensor technology, driver fatigue alerts, forklift safety zones, automated picking (to reduce manual handling risk), solar energy and electric vehicle technology, product traceability, and transport and refrigeration optimisation to reduce emissions).
- 23.3. We invest to stay at the forefront of these developments, if we do not, our business will be left behind, and our customers will be worse off as a result. More than [] is currently planned by Woolworths Group for investment into New Zealand over the next 2 years, to allow us to keep pace. [].
- 23.4. These investments carry risk, however. Our customers expect innovation, controlling rising input costs requires innovation, and historically we've known what was in our control to achieve a return and therefore secure investment funding.
- 23.5. Regulation, or the potential for regulation, will also likely depress investment in competing supply chains and alternatives by the very independent retailers and new entrants that the Commission is wanting to encourage. With no advantage to gain from moving early, independent retailers and new entrants will follow a "wait-and-see" strategy - assessing what innovations and supply-chains they may be able to access under a regulated regime, rather than developing their own version of a successful wholesale service, vertically integrated service, or supply chain.
- 23.6. Given "incumbent firms" will also be reluctant to invest (for the reasons outlined above), an investment standoff is a likely scenario, with neither "incumbent firms" or new entrants willing to make investments in innovation and new capacity that would otherwise occur in a deregulated market. Uncertainty around regulation of this type may, in fact, lessen the likelihood of more competition, investment, and capacity emerging.
- 23.7. This impact on investment is likely to the detriment of Kiwi consumers and the wider New Zealand economy. Industry needs policy settings that encourage innovation so that capital investments occur, and competition between technologies is enabled, and we get to see which delivers best for consumers. It would be in no one's interest if regulation prevented investment, new entry, and the ongoing development of effective competition. A regime that discourages investment in the food supply chain puts New Zealand at risk of supply chain breakdowns and food not being available to consumers in the event of external shocks such as natural disasters and pandemics.

24. Government investment in its own supermarket retailer

- 24.1. We already experience competition in all shapes and sizes - from green-grocers, to online supermarkets, to meal-kit providers, to competition from Costco, New World and PAK'nSAVE outlets. While we think it is unnecessary, if the Government wanted to invest in a new supermarket competitor, in our view that would be better for consumers than an intervention that undermines existing business efficiencies and incentives to invest.

25. We have an open mind to negotiating wholesale supply contracts with other retailers

- 25.1. If following the conclusion of the Market Study and sufficient time to implement and assess the impact of the other measures we support, the Commission or Government considers that additional wholesale supply would be of benefit, we have an open mind toward voluntarily negotiating commercial wholesale supply contracts with other retailers.
- 25.2. Note, while the Draft Report states we “already have the systems in place to provide wholesale grocery supply” to other retailers,¹¹² this is not the case. We are currently established as a vertically integrated business, so complexities would first need to be worked through and significant system and process overhaul and investment would be required, on longer time frames than what would be required to implement the changes we support in Parts A and B of this Submission.
- 25.3. That said, in principle we think wholesale supply is feasible. Some of the key complexities to be worked through however, would include the following:

Exhibit C4: Considerations to work through in developing a wholesale grocery business

Considerations	Details
<i>Buying and selling terms - suppliers will need to support the changes required</i>	Our supply contracts with suppliers are currently predicated on WWNZ being a retailer, with discretionary rebates (supplier promotional funding linked to retailer promotional activation) a key consideration. Discretionary rebates are a significant contributor to the net cost of goods realised by WWNZ. Specifically, discretionary rebates lower the effective cost WWNZ pays for goods by on average [] of a supplier's upfront cost (also called the “first price” or “list price”), the benefits of which flow on to consumers. Discretionary rebates are also an important competitive dynamic for suppliers, who, through these investments are able to compete with each other in categories, via promotions, to the net benefit of consumers. For WWNZ to provide wholesale supply on terms that would enable other retail customers to be competitive in the market, we would therefore need the support of our suppliers to either: • enable us to pass through suppliers' discretionary rebates to other retail customers; or • convert discretionary rebates into purchase-based fixed rebates that are embedded into the cost of goods (such a move would require the discontinuation of scan-based discretionary rebates). These would be big changes for the industry, and supplier support would be critical.

¹¹² Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [9.40].

	See Exhibit C5 below for an understanding of how significant discretionary rebates are to our cost of goods and pricing in the current operating model, and the benefits to consumers, retailers, and suppliers.
<i>Supply chain capacity - we will need to make investments</i>	We do not have excess capacity in our supply chain. At certain points of the year our packaging grocery supply chains, in particular, are already at capacity (for example, Christmas and Easter). This is before one considers the impacts of demand shocks such as COVID-19 purchasing. Therefore, to offer wholesale supply, we would have to make further investments in our supply chain to provide wholesale security of supply over-and-above the ongoing investments we are already making to meet our own requirements (for example, due to the growth of the population, which is requiring us to plan for significant further supply chain investment). That would obviously come at a cost, and we would need a return on that investment. That could be done - but it would require investment, planning, and time, as well as certainty of volume and other commitments from potential customers to support the right design of any investments.
<i>Service levels and ordering behaviour - there will need to be reasonable and mutual obligations on wholesale customers</i>	A wholesale relationship is a two-way street (see Exhibit C6 below). To make a wholesale relationship work for consumers, we need to contract with wholesale customers in a way that preserves the efficiency of current supply chains. Ad hoc purchasing behaviour, or customers without appropriate facilities to receive supply, would add cost, reduce capacity of the system, risk counterproductive outcomes, and ultimately be unworkable. Some of the more important issues we would need to factor in to the design of a wholesale business would include: • Minimum order volumes - for example, load attributes and contracted periods of supply. • Volume forecasting. • Lead time forecasting and long-term demand planning. • Agreed terms to dealing with stock shortages. • Agreed terms for damaged or rejecting stock. • Agreed terms for dispute resolution. • Agreed delivery schedules. • System requirements to enable efficient product allocation (for example, visibility into stock levels, automatic ordering). • Controlling direct access to distribution centres (DC) (including to avoid congestion and health and safety issues). • Determining whether a product is to be sold ex-DC or delivered to store. • Determining whether a customer needs to have its own cross-dock warehouse to enable safe loading zones for the unloading of goods at their stores (to meet Worksafe requirements). • Considering the bespoke requirements of each customer - for example differences in geography, differences in-store locations, differences in their own internal supply-chain capacity.
<i>Wholesale capability - we will need to make investments</i>	Our current retail franchise business is called Wholesale Distributors Limited (WDL). While the name may appear from a distance to suggest WDL is a good starting point for developing a wholesale business, that name is primarily a quirk of history as WDL had its genesis within the South Island grocery wholesaler Rattrays Wholesale Group (which included the Rattrays Cash and Carry

warehouses and tobacco vans). Today WDL is, as noted, a retail franchise business, and is not currently fit-for-purpose to become a wholesaler at scale to arms-length third-party retailers.

WDL's business is based on franchising relationships. This means:

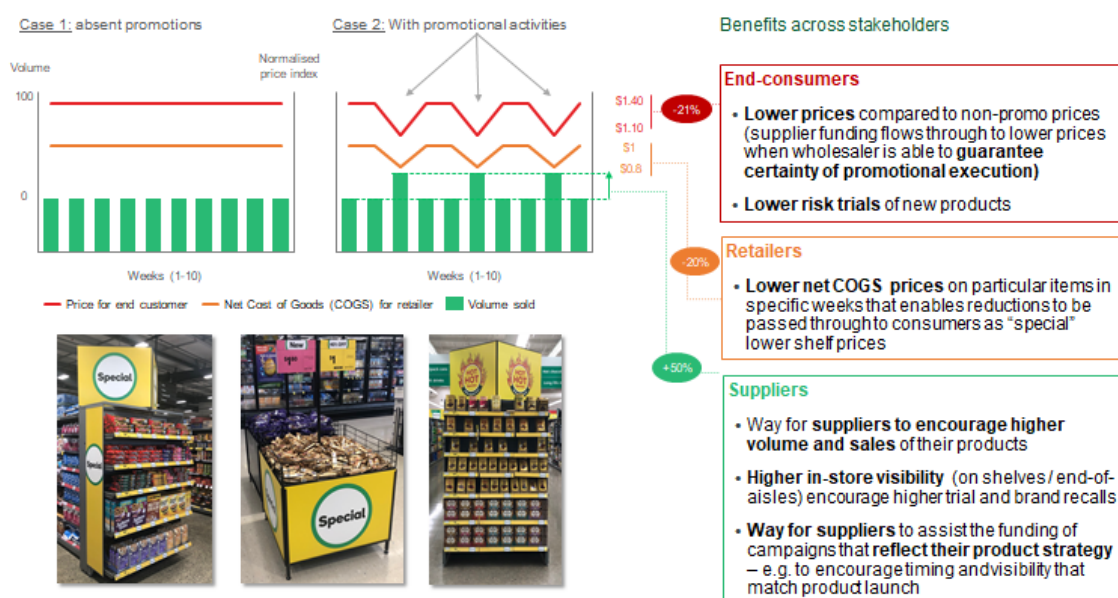
- Multiple contracts, mutual and multi-year rights and obligations that go beyond terms of supply.
- Our franchisees can access (and can choose to implement) retail promotional programmes designed by WDL - not something we could offer to arms-length third parties.
- [].

Apart from these complexities, our WDL business is sub-scale for the task of opening up supply to other third parties. Other key capabilities we would need to invest in to provide wholesale access to an appropriate standard and scale, would include (amongst other things, we are still considering):

- Wholesale sales / account management.
- Complex forecasting and demand management for wholesale customers.
- The ability to track and segregate stock differently.
- Separate wholesale pricing and costs by SKU.
- Accurate cost to serve reporting.
- New and upgraded systems and processes to support a wholesale business.

Exhibit C5: Illustrative overview of supplier funding (discretionary rebates) and the impact on pricing, benefits to consumers, retailers and suppliers

Overview of how lower COGS are negotiated with suppliers and flow through to "special" prices for consumers



- 25.4. Exhibits C6 and C7 below illustrate a number of the points outlined above - demonstrating the need for flexibility to negotiate fit for purpose contractual arrangements, consistent with a two-way partnership that is customised to different retailer models and needs.

Exhibit C6: Wholesale-retailer relationships and the need for reciprocal obligations¹¹³

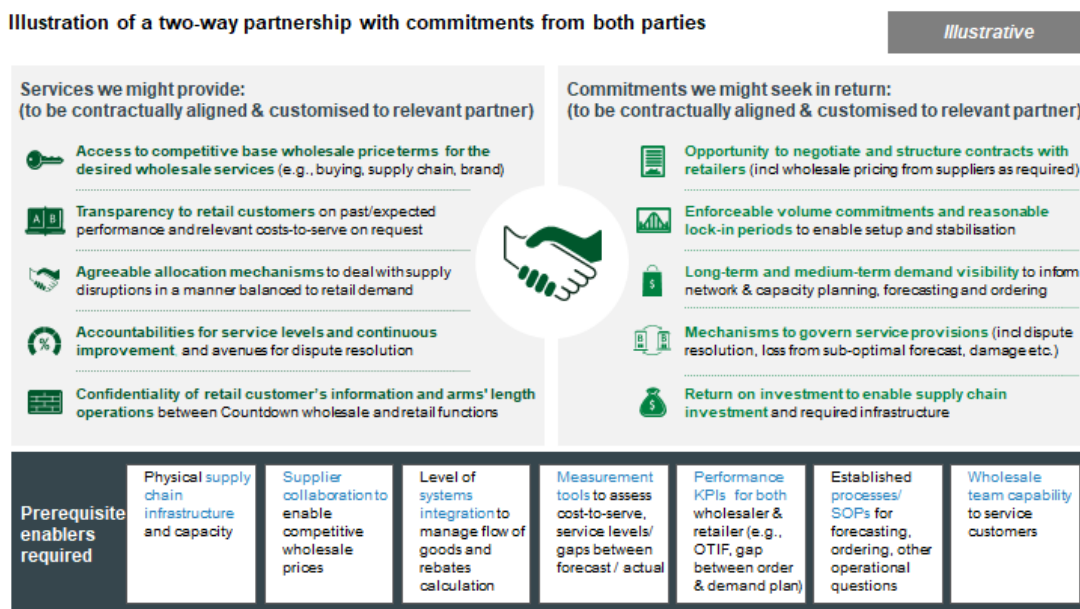


Exhibit C7: overview of different wholesale requirements by type of retail customer

Overview of different wholesale requirements that might be agreed depending on type of retail customer *Illustrative*

	Large retailer	Group of independents	Independent retailer
Potential options for wholesale services that might be agreed:			
None • Retailer prefers dealing direct with a supplier	✓	✓	✓
Pure wholesale buying services • Buying support to access base wholesale prices and volume rebates	✓	✓	
Cash and carry • Buying support and storage support in a DC		✓	
Supply chain services • Buying support and supply chain services to deliver to store	✓	✓	✓
Supply chain services and stock management • All of the above along with services to provide integrated forecasting and ordering systems for more optimal flow of goods		✓	✓
Opt-in branding arrangements • A Supply chain services model and standardized brand banners • Optional marketing strategies, operations, IT, compliance support		✓	✓
Controlled branding arrangements (including e.g. franchising) • All of the above with additional store support (e.g., training, store operations support on POS tools, pricing, IT, analytics) and greater co-investment into retailers and paying for rental of select premises, advertising materials etc.			✓

- 25.5. Overall, despite the complexities, if following the Market Study and a sufficient passage of time to implement and assess the impact of the other options we support, the Commission or

¹¹³ On products outside of exclusions listed. Dependent on the nature of wholesale services being provided.

Government considered that additional wholesale supply would be of benefit, we would be open to offering competitive commercial wholesale arrangements with other retailers. That would require time frames longer than what would be required to implement the changes we support in Parts A and B of this Submission.

25.6. In terms of scope, our view is that voluntary arrangements would be in relation only to those products that the Commission has indicated it has concerns with not being currently wholesaled by independent wholesalers (for example, packaged groceries), where those retailers also:¹¹⁴

25.6.1. fall within the definition of the types of retailers that the Commission has indicated it wants to see emerge as new competitors (for example, “main shop” bricks-and-mortar retailers); and

25.6.2. meet certain minimum service level requirements to be a viable wholesale customer - for example, minimum order volumes, order forecasting, health and safety, and other important considerations.

25.7. Even with these complexities, this is still clearly a preferable option (for WWNZ, the sector, consumers and taxpayers) than some of the other more interventionist options the Commission may be considering - particularly given there are, in our view, significant questions and issues with respect a number of the Commission’s preliminary findings. We retain an open mind to negotiating wholesale supply contracts with other retailers, if necessary, and look forward to discussing further with the Commission, if required, over time.

¹¹⁴ The Draft Report noted that options for independent wholesale supply to independent retailers already exist for meat and produce and some imported products (see paragraph 6.127 of the Draft Report). While the Draft Report cited examples such as T&G Fresh and MG Marketing (in fresh produce), the wholesalers listed on the Beef+Lamb New Zealand Website (in meat), and AB International, Acorn Group, Tai Ping, Asian Savour (in imported products), the Draft Report should have also specifically cited that a number of other products are typically supplied by suppliers through a “direct store delivery” (**DSD**) model, whereby the supplier picks store specific orders and deliver directly to stores - including to numerous supermarkets, service stations, convenience stores, and dairies. The DSD model is often used for products with shorter shelf life (such as bread, milk, and meat) and, therefore, such products do not use or rely on the grocery retailer’s supply chain. Therefore, even taking the Draft Report’s preliminary finding that entry by new grocery retailers is dependent on a grocery wholesaler (which we do not consider is correct), the Draft Report’s preliminary finding is the potential “gap” in relation to wholesaling is limited to long-life packaged products. Therefore, even adopting the Draft Report’s preliminary finding, we could not see a need for WWNZ to enter into commercial wholesale arrangements with other retailers in relation to such products - i.e. fresh produce, meat, imported products, milk, bread, or other DSD products that already catered for by a large number of other wholesalers and suppliers with their own distribution networks.

Part D: Our view on the Draft Report's preliminary findings

We know this Market Study is important to New Zealanders, and so we want to help the Commission get it right. There is too much at stake if the findings are incorrect, overstated, or if recommendations are made that are not based on fact or are ill-conceived. Given there are a number of preliminary findings in the Draft Report that we disagree with, our view is the Commission needs to revisit a number of aspects of its analysis and findings prior to publication of its Final Report. Our views on those preliminary findings are set out in this Part D.

26. Grocery prices in New Zealand do not suggest that there is an issue with competition

The Commission's Draft Report places great weight on trying to compare New Zealand's retail grocery prices to other countries, and then using those comparisons to make findings about competition here. However, making accurate comparisons is not easy. Our view is that there are problems with the Draft Report that mean the comparisons it has made are not accurate, and its preliminary findings about competition are not supported.

26.1. Retail grocery food prices have fallen in real terms:

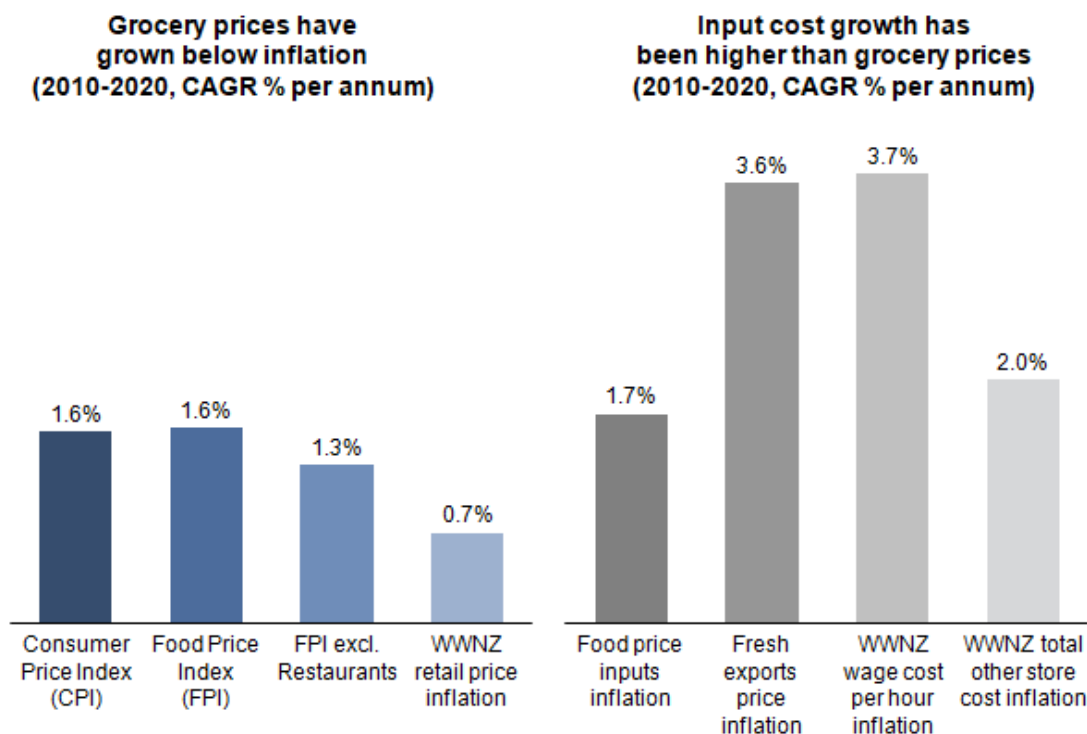
- 26.1.1. The Draft Report states that "a firm in a workably competitive market will find it hard to raise prices",¹¹⁵ and that in markets where "competition is less intense" grocery retailers would have an incentive to increase prices.¹¹⁶ We agree, which is why we consider the fact that retail grocery food prices have decreased in real terms (that is, grown more slowly than CPI, as well as most input costs) over the last decade should have been a key feature in the Draft Report.
- 26.1.2. Falling retail grocery food prices (in real terms) is a key indicator that competition is intense, and working for consumers. We have worked hard over the last decade to restrict retail price inflation at Countdown to 0.7% per annum (well below CPI of 1.6% per annum and input cost increases of 1.7% to 3.7% per annum). If competition was not working in the sector, then increasing input costs would have been not only passed through to consumers, but more than passed through. This has not occurred. Instead, competition has fueled efficiency - reduced stock loss, improved supply chain productivity, and improved in-store processes - lowering costs, while delivering competitive prices.¹¹⁷

¹¹⁵ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [5.28].

¹¹⁶ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [4.51].

¹¹⁷ For these reasons, in our view the fact that the retail grocery food prices have fallen (in real terms) over the last decade, despite increasing input costs, demonstrates that the Draft Report's statement (at [3.172]) that it is not clear "that consumers are benefitting from [supply-chain] cost saving investments" is incorrect.

Exhibit D1: Changes in grocery prices versus CPI (2010 - 2020)



26.2. There are difficulties in making international comparisons and these have been understated by the Commission:

- 26.2.1. We outlined in our Initial Submission the significant difficulties in trying to make international comparisons of grocery prices, which mean that such comparisons are unlikely to be able to be made in any meaningful or informative way and risk being misinterpreted.¹¹⁸ This was recognised by the UK Competition Commission in its 2007 grocery market study:¹¹⁹

“International comparisons of prices are difficult to make as a result of exchange rate issues, comparability of products and pack sizes, the role of tax in food prices, and different property markets and planning regimes. For these reasons, we consider that the value of any extensive cross-country comparison would be limited.”

- 26.2.2. Those difficulties include the following:

- 26.2.2.1. Difficulty in standardising the non-price dimensions of products whose prices are being compared - for example, differences in quality between produce products and differences in pack sizes. This was recognised by the ACCC in its grocery market study, noting that “differences in quality of goods are not sufficiently reflected across countries”.¹²⁰

¹¹⁸ WWNZ submission on the Preliminary Issues Paper - 4 February 2021. Response to Question 20.

¹¹⁹ UK Competition Commission Provisional findings report. The Supply of Groceries in the UK market investigation (October 2007). Page 27.

¹²⁰ ACCC. Report of the ACCC inquiry into the competitiveness of retail prices for standard groceries. (July 2008). Page 25.

- 26.2.2.2. Differences in the availability of products, and the distance to market for products, in different jurisdictions. For example, grapes may be domestically grown in the US and imported in New Zealand (or vice versa), which impacts the underlying costs of bringing products to market.
- 26.2.2.3. Difficulty in standardising the period of measurement, for example differences in seasons and availability of products and when the period of measurement commences. This was also recognised by the ACCC in its grocery market study, noting that “international comparisons are ‘highly susceptible to price level variations at the commencement of the period under study, since it is easier to make percentage gains off a low base than a high one’”.¹²¹
- 26.2.2.4. Differences in economic performance and inflation rates in different jurisdictions.
- 26.2.2.5. Differences in input costs such as:
 - 26.2.2.5.1. differences in transport costs due to different physical geography, population density and population dispersal. For example, the 2012 Productivity Commission inquiry into international freight transport found that the cost of container shipping prices for imports into Auckland were considerably higher than Sydney, with import shipping costs in Auckland from port to port 30% more expensive than Sydney in the Productivity Commission case studies.¹²² Furthermore, data from the EU and New Zealand on the average load carried by heavy road vehicles in 2017 show that New Zealand has relatively low vehicle loads when compared to average freight loads in EU countries;¹²³
 - 26.2.2.5.2. differences in minimum wages and employee entitlement costs; and
 - 26.2.2.5.3. differences in electricity costs.
- 26.2.2.6. Differences in seasonality, demand, and weather events or supply issues in relation to the supply of certain products (for example, a hail storm at harvest time or drought in New Zealand).
- 26.2.2.7. Exchange rate issues.
- 26.2.2.8. Differences in tax rates, including:

¹²¹ ACCC Final Report. Report of the ACCC inquiry into the competitiveness of retail prices for standard groceries (July 2008). Page 25.

¹²² New Zealand Productivity Commission. International Freight Transport Services Inquiry: Final report (April 2012). Pages 4 - 5 and 84.

¹²³ Data for New Zealand obtained from the Ministry of Transport, available at: <https://www.transport.govt.nz/statistics-and-insights/fleet-statistics/sheet/heavy-vehicles>. Data for EU countries obtained from Eurostat, available at: https://ec.europa.eu/eurostat/statistics-explained/index.php/Road_freight_transport_by_journey_characteristics#Average_vehicle_loads

- 26.2.2.8.1. differences in GST rates and the application of GST to food products; and
- 26.2.2.8.2. differences in fuel taxes, and road user charges.
- 26.2.2.9. Differences in accounting treatments between different grocery retailers mean that it is not possible to make a meaningful or informative comparison of metrics such as gross profit rates.
- 26.2.2.10. Differences in regulatory settings, including differences in subsidies (or lack thereof) on different products, differences in import / export restrictions on certain products, and / or differences in the need for quarantining or other biosecurity treatment of products (for example, irradiation or chemical treatment of imported produce into New Zealand).
- 26.2.2.11. Differences in business models - for example, whether retailers own or lease their premises. The ACCC recognised in its grocery market study that “[t]he issue of leasing versus owning buildings may also affect international EBIT comparisons”.¹²⁴
- 26.2.2.12. Differences in the range of activities, in addition to grocery retailing, conducted by retailers will impact factors such as pricing and margins. This was recognised by the ACCC in its grocery market study, noting that for this reason “[l]ike-for-like comparisons are not straightforward”.¹²⁵
- 26.2.3. The Draft Report, unlike the approach of the UKCC¹²⁶ and ACCC, understated these difficulties and, therefore, placed too much (and incorrect) weight on comparisons.

26.3. There are also clearly many other factors beyond competition at play:

- 26.3.1. New Zealand is an expensive place overall: The same OECD dataset and approach used by the Commission suggests that New Zealand has a comparatively high price ranking for a number of goods and services, across a number of sectors, not just groceries (see Exhibit D2). This reflects that New Zealand presents its own unique challenges, including being:
 - 26.3.1.1. small (our total population is smaller than the population of Sydney);
 - 26.3.1.2. geographically distant from other countries (which means more expensive freight costs, longer lead times, and the requirement for more extensive inventory management for imports);¹²⁷ and

¹²⁴ ACCC. Report of the ACCC inquiry into the competitiveness of retail prices for standard groceries. (July 2008). Page 25

¹²⁵ ACCC. Report of the ACCC inquiry into the competitiveness of retail prices for standard groceries. (July 2008). Page 25

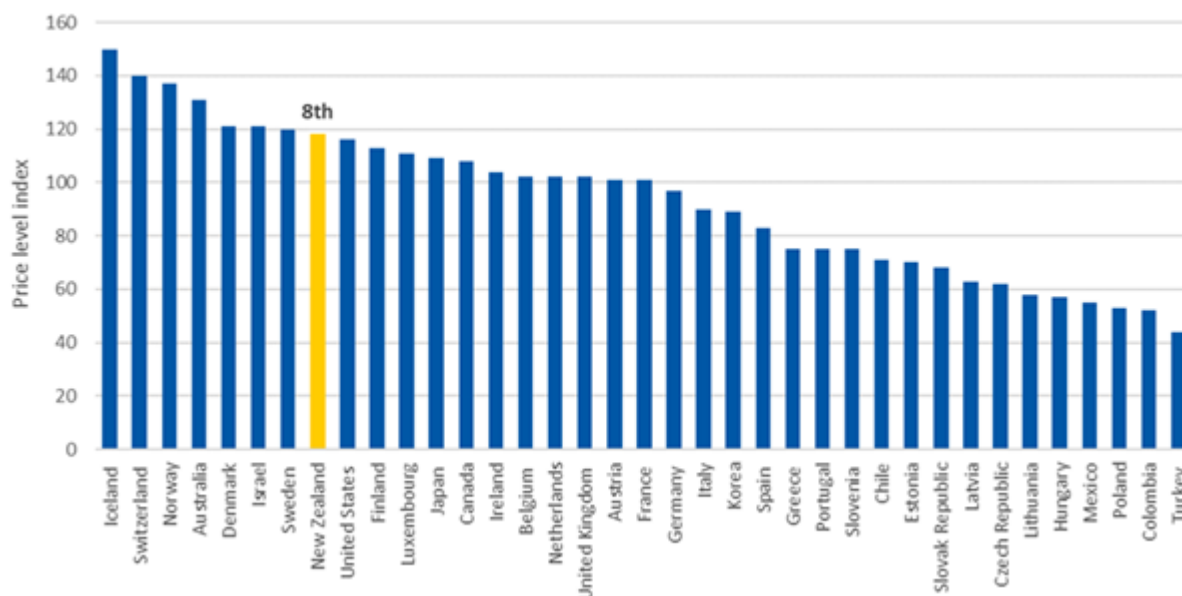
¹²⁶ Now part of the UK Competition and Markets Authority (CMA).

¹²⁷ The 2012 Productivity Commission inquiry into international freight transport found that the cost of container shipping prices for imports into Auckland were considerably higher than Sydney, with import shipping costs in Auckland from port to port 30% more expensive than Sydney in the Productivity Commission case studies. New Zealand Productivity Commission, *International Freight Transport Services Inquiry: Final report*, April 2012, p 4 - 5 and 84.

26.3.1.3. geographically dispersed (including across several islands) with lower population density,¹²⁸ lower average vehicle freight loads than many other countries (which means more expensive distribution costs within New Zealand).¹²⁹

The Draft Report does not acknowledge that New Zealand has a comparatively high price ranking for a number of goods and services, across a number of sectors. This is a significant (and omitted) fact, when it comes to assessing the role of competition as a driver of grocery prices. Clearly, other dynamics are at play.

Exhibit D2: Economy-wide price levels (2017)¹³⁰



26.3.2. Different input costs can be a significant factor: For example, analysis by Woolworths Group on the subset of ~7,500 identical (barcode matched) longlife grocery and general merchandise products that are stocked in both WWNZ and Woolworths Australia shows that WWNZ has to pay approximately 10% more on average for these same products than Woolworths Australia (these figures exclude GST). Despite this, WWNZ on average sells these products at a similar retail price (again,

¹²⁸ The draft report noted that New Zealand's population density was half that of the OECD average (paragraph 6.40.1).

¹²⁹ Data from the EU and New Zealand on the average load carried by heavy road vehicles in 2017 show that New Zealand has relatively low vehicle loads when compared to average freight loads in EU countries. Data for New Zealand obtained from the Ministry of Transport, available at <https://www.transport.govt.nz/statistics-and-insights/fleet-statistics/sheet/heavy-vehicles>. Data for EU countries obtained from Eurostat, available at https://ec.europa.eu/eurostat/statistics-explained/index.php/Road_freight_transport_by_journey_characteristics#Average_vehicle_loads

¹³⁰ OECD.Stat, 2017 PPP Benchmark results, Table 1.11: Price level indices (OECD=100).

excluding GST).¹³¹

- 26.3.3. GST on food is high in New Zealand: New Zealand is an outlier in taxing groceries at the same rate (15%) as other goods and services.¹³² Australia exempts fruit and vegetables, meat, and most basic foods from their GST rate of 10% and the UK exempts most food from VAT. GST is likely making a far larger difference to the prices of groceries in New Zealand than supermarket profits.
- 26.3.4. Tobacco and alcohol taxes and excise: Tobacco and alcohol are both taxed heavily in New Zealand, with tobacco taxes and excises particularly high compared to most other countries.¹³³ While referenced as being of relevance in the Draft Report, they are not accounted for in the Commission's substantive analysis.
- 26.3.5. Even if our business made no profit, this would still not change New Zealand's food price ranking in the eyes of the Commission: We are highly focused on controlling costs to help deliver competitive prices, including reduced stock loss, improved supply chain productivity, and improved in-store processes. Our margins are 2.4c in \$1 spent.¹³⁴ Even if we made no profit at all, New Zealand's price ranking (based on the Commission's view) would still not change relative to the rest of the world.¹³⁵ Other commentators have noted this also.¹³⁶
- 26.3.6. There is no relationship between the Commission's international price comparisons and the returns of major grocery retailers: Based on the Commission's own international comparison sample, grocery retailer returns do not appear to have any relationship to grocery retail prices (as illustrated in Exhibit D3). This suggests that other factors are likely to be far more significant in contributing to prices in those countries or that there are measurement problems with the Return on Average Capital Employed and / or the price indexes.

¹³¹ This comparison has been performed by adjusting for exchange rate differences (using the average exchange rate for the period). These common barcode matched products represent a subset of longlife products equivalent to approximately [] of Countdown's total sales value. Woolworths Australia ultimately has very similar EBIT margin outcomes as WWNZ as a result of higher costs in some other areas (and to a lesser extent other mix dynamics), and operates in a grocery market with Coles, Aldi, Metcash/IGA, Costco and now Amazon that is acknowledged as being "highly competitive" (for example, Bankwest Future of Business: Focus on Supermarkets Report (2019). Available at:

<https://www.bankwest.com.au/content/dam/bankwest/documents/business/insights/focus-on-supermarkets-report-2019.pdf>

¹³² (28 April 2008). Removal of GST on food unlikely - PM. NZ Herald. Retrieved from:

<https://www.nzherald.co.nz/nz/removal-of-gst-on-food-unlikely-pm/GUQOBX2ONXIL7EYLG7DHQTUEKA/>

This article noted:

Examples of GST treatment of food:

Most food exempt: Britain, Ireland

Basic foods exempt: Australia, Canada, Mexico, South Korea.

Food taxed at lower rate: Austria, Belgium, Czech Republic, Finland, France, Greece, Hungary, Iceland, Italy, Luxembourg, Netherlands, Norway, Poland, Portugal, Slovakia, Spain, Sweden, Switzerland, Turkey.

Food taxed at same rate as other goods: Denmark, Japan, **New Zealand**.

No GST: United States.

¹³³ OECD, Consumption Tax Trends 2020: VAT/GST and Excise Rates. Trends and Policy Issues, Annex 3.A.

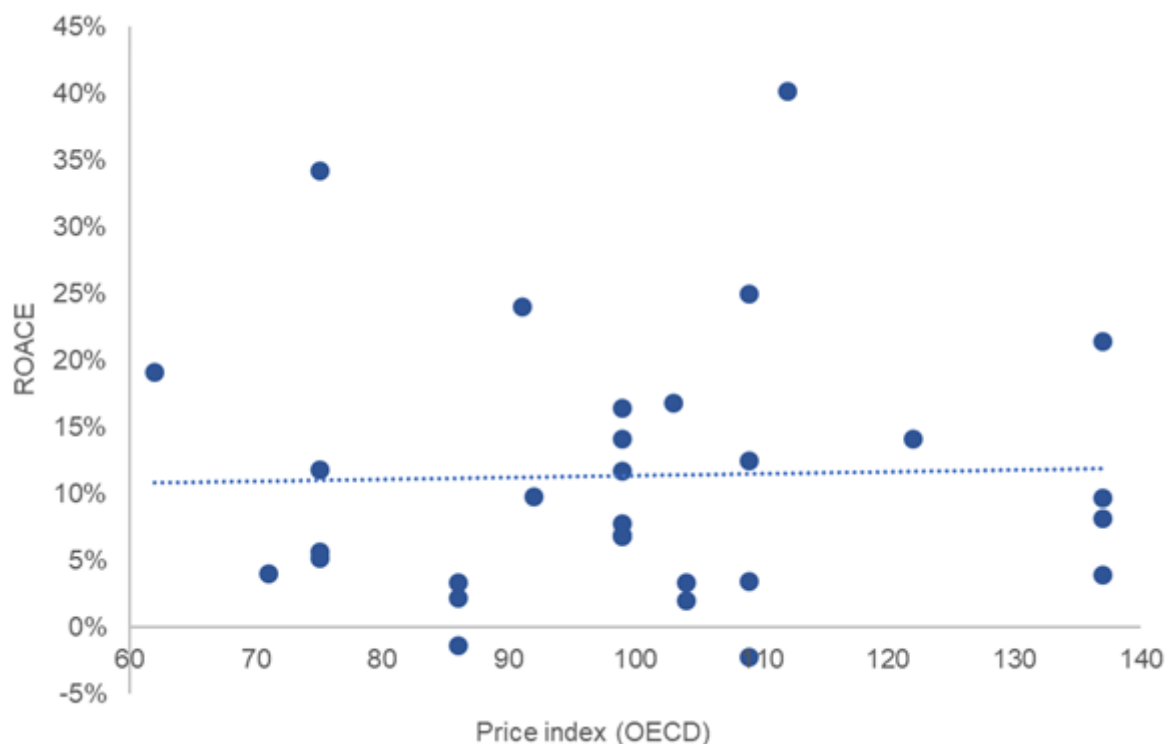
¹³⁴ FY2020.

¹³⁵ Analysis by WWNZ and NERA Economic Consulting Ltd.

¹³⁶ (15 August 2021). Commerce Commission's supermarket report reveals lack of competition is 'trivial'. Stuff Retrieved from:

<https://www.stuff.co.nz/national/politics/opinion/300381939/commerce-commissions-supermarket-report-reveals-lack-of-competition-is-trivial>

Exhibit D3: Average Return on Average Capital Employed (2015-2019) and the food and beverage OECD price level index (2017) for comparator companies

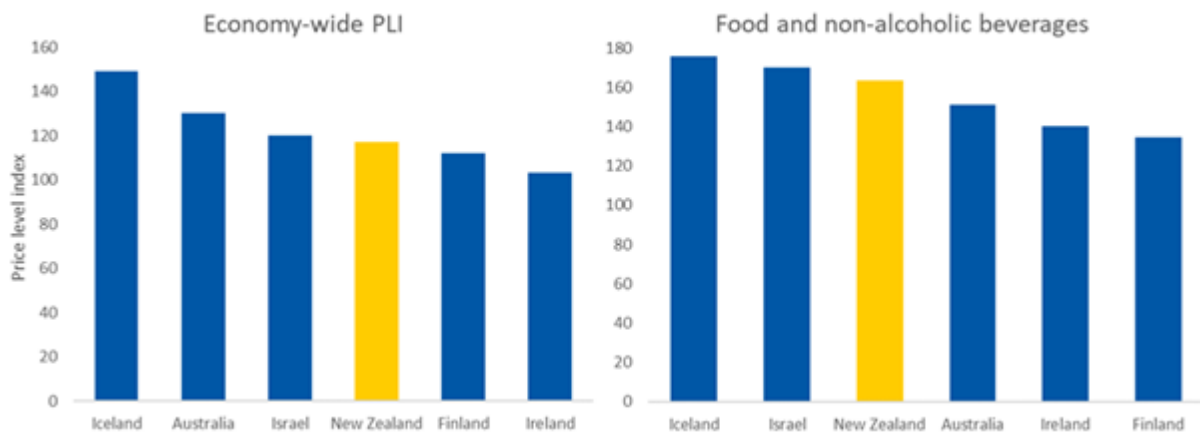


26.3.7. Adopting the Commission's own comparisons, New Zealand's grocery prices are not high compared to other countries like us: In the Draft Report the Commission said it had compared New Zealand's grocery prices to smaller subset of countries "comparable to New Zealand in terms of scale and size"¹³⁷ and found that New Zealand's prices are "higher than the average for this smaller comparator group".¹³⁸ We do not think the Commission's commentary on that analysis gave an accurate picture. That analysis showed that, compared to this subset of comparable countries, New Zealand's grocery prices are in the middle of the pack when looking at food and non-alcoholic beverages, and where you would expect them to be in comparison to how pricing levels in New Zealand across all sectors compare to other countries (even before you take into account all the other relevant factors, such as New Zealand's distance from other markets, population density, and other things). See Exhibit D4 below. Therefore, the Commission's analysis did not show high prices in New Zealand compared to these other countries.

¹³⁷ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [3.113].

¹³⁸ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [3.115].

Exhibit D4: Comparing economy-wide price levels and grocery price levels between a subset of countries “similar to New Zealand” (2017)¹³⁹

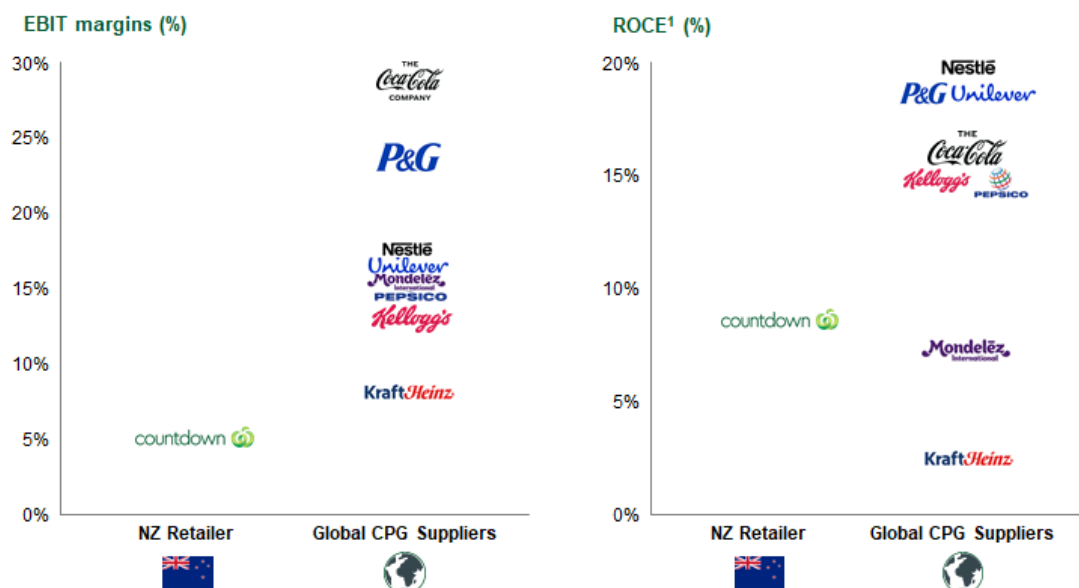


- 26.3.8. Multinational supplier margins have a greater impact than retailer margins: For every \$1 spent by a customer in a supermarket, we pay 63 cents directly to our suppliers, and the evidence is that supplier profits are making a higher contribution to the prices of groceries in New Zealand than grocery retailers' returns. Demonstrating this, in many categories a small number of multinational suppliers account for 60% to 90% of products sold (for example, Unilever, Coca-Cola Amatil, Nestle, Procter & Gamble, Pepsico, Mondelez and others), and those suppliers typically have EBIT margins in the range of 10% to 30% (compared to WWNZ with around 5.0%) and a pre-tax Return of Capital Employed of 10% to 40% (compared to WWNZ with pre-tax Return of Capital Employed around 8% to 9%). See Exhibits D5 and D6 below.

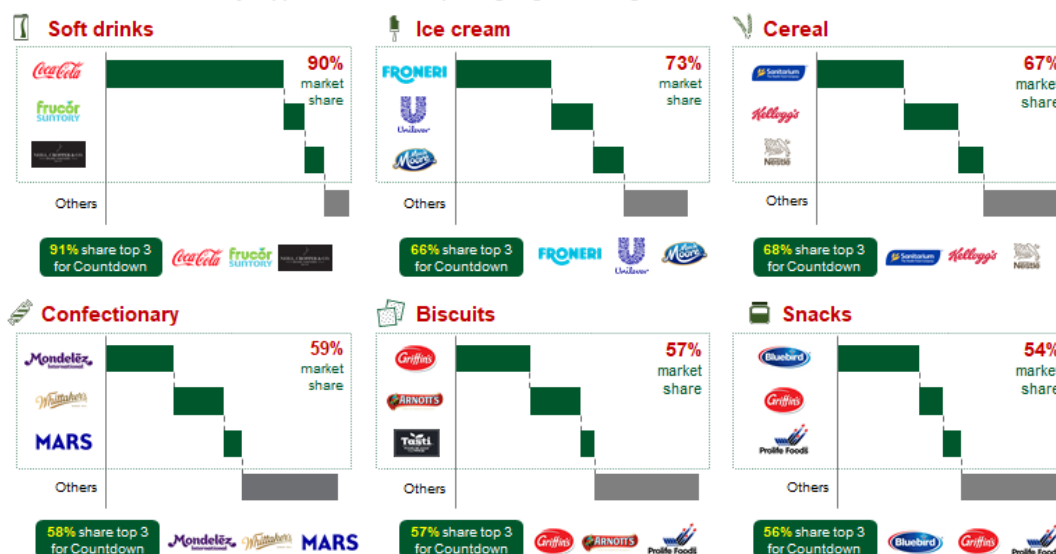
¹³⁹ OECD.Stat, 2017 PPP Benchmark results, Table 1.11: Price level indices (OECD=100).

Exhibit D5: Supplier margins and returns are higher than retailer margins and returns¹⁴⁰

Supplier vs Retailer comparison based on reported financial returns

Exhibit D6: Concentration of multinational suppliers in key product categories¹⁴¹

Share of 2020 revenues by suppliers in selected packaged goods categories



26.3.9. International commodity markets and export prices have a significant impact on our input costs: In New Zealand, export markets are by far the biggest market for many of our farmers and growers, with the local consumer market being only a small

¹⁴⁰These Returns on Capital Employed metrics are calculated using a different methodology to the Commission in the Draft Report. They are based on Orbis database calculations using the standardised formula of (P/L before tax + Interest paid) / (Shareholder funds + non-current liabilities). WWNZ numbers are calculated by applying the same formula to the adjusted financials (post removal of non-grocery items) to enable a like for like comparison. Note: returns are based on closing capital position as of year-end (not average); in all cases margin and returns are based on the latest available financial results (FY20). Source: Orbis, WWNZ adjusted financials.

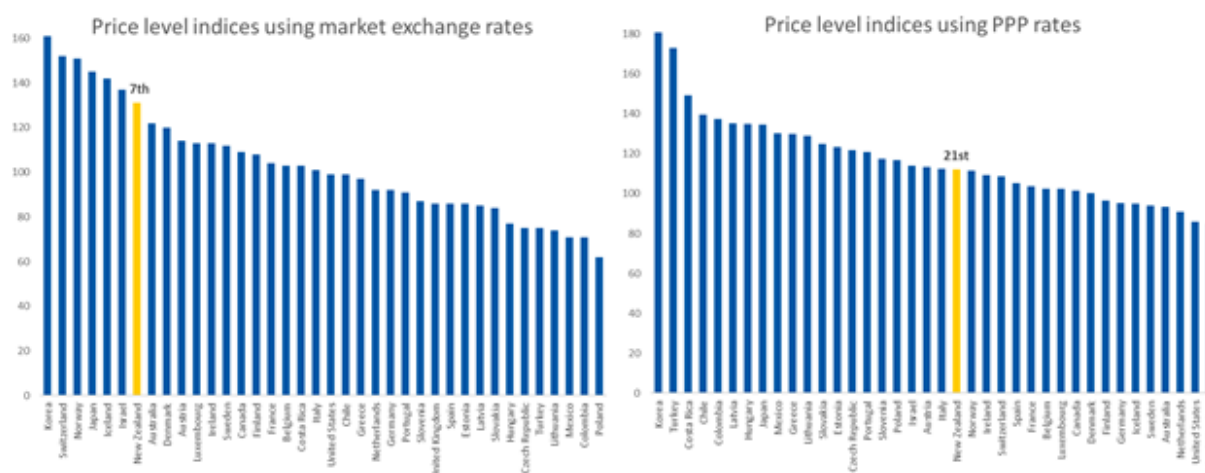
¹⁴¹ Market data based on IRI pre-packaged data; Countdown data.

proportion of their supply.¹⁴² This means that export prices for key New Zealand grocery exports (dairy, meat, fish, and fruits and vegetables),¹⁴³ which have generally been increasing over the last decade, inevitably put additional upward pricing pressure on our input costs given that in New Zealand we need to purchase these products, in effect, at prices equivalent to those our suppliers can obtain on the export market. The Draft Report did not address this.

26.4. There are also other issues with the Commission's price comparisons:

26.4.1. The Commission did not use a price purchase parity (PPP) approach to compare prices between countries, nor sensitivity test using a PPP approach (both of which it would ordinarily do in comparing prices between countries):¹⁴⁴ If it had used PPP, instead of New Zealand prices appearing to be sixth in the OECD, making no other adjustments, New Zealand drops to twenty-first - see Exhibit D7 below.

*Exhibit D7: Price comparisons of food and non-alcoholic beverages under different exchange rate assumptions (2017)*¹⁴⁵



¹⁴² For example, as noted in our Initial Submission:

- 95% of lamb and mutton production is exported;
- 95% of dairy production is exported;
- 94% of kiwifruit production is exported;
- 90% of onion production is exported;
- 88% of beef and veal production is exported;
- 77% of wine is exported;
- 73% of venison production is exported;
- 66% of apple production is exported (just 13% is consumed domestically in unprocessed form, with ~20% used for on-processing);
- 54% of avocado production is exported;
- 45% of seafood production is exported;
- 44% of honey production is exported; and
- 37% of pear production is exported.

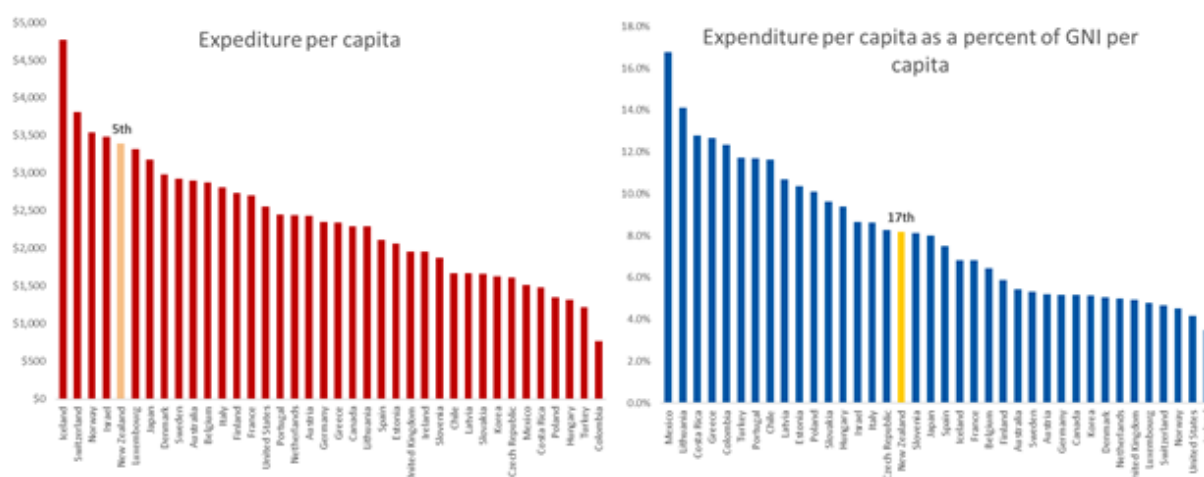
¹⁴³ Which, according to Statistics NZ data, comprise 39% of New Zealand's estimated household grocery expenditure in the year ending June 2019.

¹⁴⁴ As it did in its Mobile Market Study, amongst other benchmarking analyses. (26 September 2019). See: https://comcom.govt.nz/_data/assets/pdf_file/0022/177331/Mobile-Market-Study-Findings-report-26-September-2019.PDF

¹⁴⁵ The price level indices using market exchange rates can be interpreted as the price levels of food and non-alcoholic beverages relative to other countries, while the price level indices using PPP rates can be interpreted as the price levels for food and non-alcoholic beverages relative to general price levels for that economy (that is, an index over 100 means price levels are above general price levels in that economy). OECD.Stat, 2017 PPP Benchmark results, Table 1.11: Price level indices (OECD=100).

- 26.4.2. There is no evidence that New Zealanders spend a relatively high proportion of their income on groceries: The Draft Report states that “New Zealanders appear to spend a relatively high proportion of their income on groceries”.¹⁴⁶ However, the Draft Report did not include any analysis of grocery expenditure compared to income and, therefore, there is no basis or evidence for that statement. When food expenditure is instead looked at as a proportion of gross national income levels, New Zealand drops to seventeenth in the OECD - see Exhibit D8 below.

Exhibit D8: Expenditure per capita on food and non-alcoholic beverages alone and as a percent of GNI per capita using market exchange rates (2017)¹⁴⁷



- 26.4.3. We do not see why the Commission dismissed the EIU data: That data indicated that retail grocery prices in New Zealand are not high compared to other OECD countries. As outlined further in the NERA report **enclosed**, we consider that EIU data is just as valid as other measures included in the Draft Report.¹⁴⁸ In particular:

- 26.4.3.1. The Draft Report provides no evidence as to why datasets produced by national statistical agencies can, or should, be regarded as more accurate than data collated by a private organisation such as EIU.¹⁴⁹ EIU data is relied upon by a range of global companies, the financial sector, governments and academic institutions around the world, and the EIU is regarded as “the world’s foremost provider of country, industry and

¹⁴⁶ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [3.20].

¹⁴⁷ World Bank, ICP 2017 results and World Bank DataBank, World Development Indicators.

¹⁴⁸ We also note that the Draft Report (at [3.83.3]) included reference to “preliminary analysis by Coriolis saying that there is a price difference between New Zealand and the US of 2-6% that is driven by competition factors”. We have previously provided the Commission with NERA analysis outlining why the Coriolis chart is “purely stylistic, with no references to evidence, data or quantification to support the claimed components (including their size)” and, therefore, “is of no informative value”. It is unclear, given the Commission has not been provided any evidence underlying the Coriolis chart, why it considers it appropriate to place more weight on that Coriolis chart (by citing it at [3.83.3]) than NERA’s analysis of the EIU data (which was analysed rigorously, with the underlying data and method provided to the Commission). The Commission also appeared to place weight on a submission by The Warehouse that “[The Warehouse] understands that New Zealanders pay high grocery prices in New Zealand compared to other international markets” by citing that at [3.83.1], without any evidence or data underpinning that statement by The Warehouse.

¹⁴⁹ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [3.130].

management analysis.”¹⁵⁰ In addition, the ICP and OECD datasets used by the Commission are aggregate indices to broad category levels, which cannot be used for the type of product-level price comparisons NERA has done.

26.4.3.2. We do not agree with the Draft Report’s dismissal of NERA’s use of PPP to compare prices between jurisdictions. That is the very approach the Commission adopts for comparing the price of other goods / services between jurisdictions - for example, noting in its 2020 Annual Telecommunications Monitoring Report that the use of PPP is “generally accepted as an appropriate conversion method for non-tradable goods and services.”¹⁵¹ The World Bank’s International Comparison Programme, a worldwide statistical initiative to collect comparative price data, notes: “Purchasing power parities allow comparisons between economies of expenditure shares or price levels for components such as food, health care, and investments.”¹⁵² The Commission’s dismissal of PPP on the basis that grocery products are “tradeable” is incorrect.¹⁵³ Statistics New Zealand defines the “supermarket and grocery stores” industry as “non-tradable”.¹⁵⁴

26.4.3.3. We do not agree with the Draft Report’s critique of NERA’s use of a ranking methodology on the basis that the “ranking mechanism may limit the influence over very cheap or expensive goods”.¹⁵⁵ That is not a valid criticism of the methodology used by NERA. The methodology used by NERA explicitly takes into account that consumers buy a range of items, which is why the distribution of product price rankings is shown. Moreover, the ranking methodology does not give more weight to more expensive or less expensive items so that it does not skew the relative levels when these items may have different levels of importance across economies.¹⁵⁶

26.4.4. For these reasons, our view is that the price comparisons made in the Draft Report do not provide reliable evidence of a lack of competition in the New Zealand grocery industry, and therefore cannot be relied upon as justification for intervention, especially for some of the more extreme options put forward. We ask the Commission to consider and address each of these concerns in the Final Report and appropriately qualify any findings relating to price comparisons.

¹⁵⁰ Economist Intelligence Unit, “Setting the standard for country analysis and forecasting”. Available at: http://graphics.eiu.com/files/ad_pdfs/2005Methodology.pdf

¹⁵¹ Commerce Commission “Annual Telecommunications Monitoring Report - 2020 Key Facts (16 March 2021). Page 28 (see “List of defined terms”). Available at: https://comcom.govt.nz/_data/assets/pdf_file/0030/247377/2020-Annual-Telecommunications-Monitoring-Report-Revised-version-16-March-2021.pdf

¹⁵² The World Bank, “2005 International Comparison Program - Global Purchasing Power Parities and Real Expenditures” at page 5. Available at: <https://thedocs.worldbank.org/en/doc/982121487105148964-0050022017/original/2005ICPReportFinalwithNewApgG.pdf>

¹⁵³ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [3.90].

¹⁵⁴ Statistics NZ, The tradable sector and its relevance to New Zealand’s GDP, 3 July 2013, p 28.

¹⁵⁵ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [3.125].

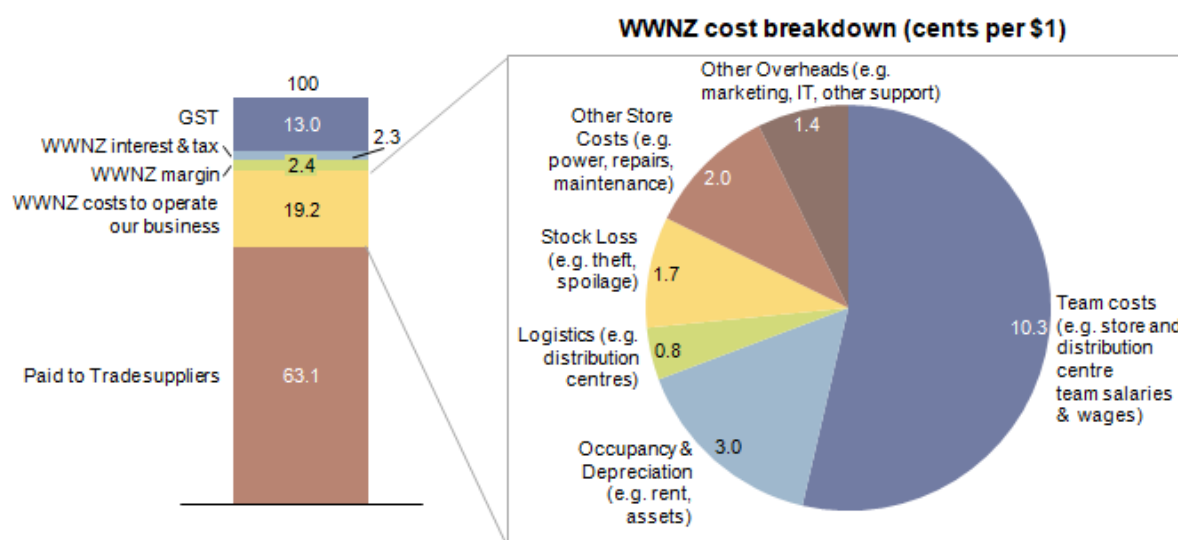
¹⁵⁶ For example, the enclosed NERA Report states: “...the price level ranking for rice and the price level ranking for steak are given the same weight. A country which, on balance, has more items which cost less money than the equivalent item in a comparator country (regardless of the importance of that item in the country’s culture or relative price difference between the items) will rank lower than that country.”

27. Supermarket returns in New Zealand do not suggest there is an issue with competition

We disagree with the views expressed in the Draft Report that supermarket returns in New Zealand suggest there is an issue with competition.

- 27.1. **We are a low-margin business (2.4 cents in every dollar spent in our stores):** Reflecting the competitive prices we offer to Kiwis, we are a low-margin business. WWNZ's margin is 2.4 cents in every dollar spent at our supermarkets.¹⁵⁷ This is because, for every \$1 spent in a supermarket, we pay 63 cents directly to our suppliers, 19 cents relates to the costs of running our supermarkets, supply chain and paying our team, 13 cents is GST, and 2 cents is interest and other tax costs. See Exhibit D9 below.

*Exhibit D9: Component breakdown of consumer grocery price at WWNZ
(cents per \$1)*



- 27.2. **Our margins and returns are lower than Woolworths in Australia:** We are part of the publicly-listed Woolworths Group, so we measure and report a number of comparable financial measures across our New Zealand and Australian businesses. This shows that in FY2019 that EBIT margins (New Zealand 4.4%, Australia Food 4.6%), gross profit margins (New Zealand 24.4%, Australia Food 28.7%) and pre-tax Return on Funds Employed (New Zealand ~9%, Australia Group ~14%) are equivalent to or lower for WWNZ than Woolworths in Australia. Given the Australian market is considered “highly competitive”,¹⁵⁸ this means either that our returns are consistent with high levels of competition, or that no meaningful conclusions can be drawn from comparisons of returns.
- 27.3. **Our margins and returns are much lower than many of our multi-national suppliers:** As noted at paragraph 26.3.8 above, many of our multinational suppliers have larger EBIT

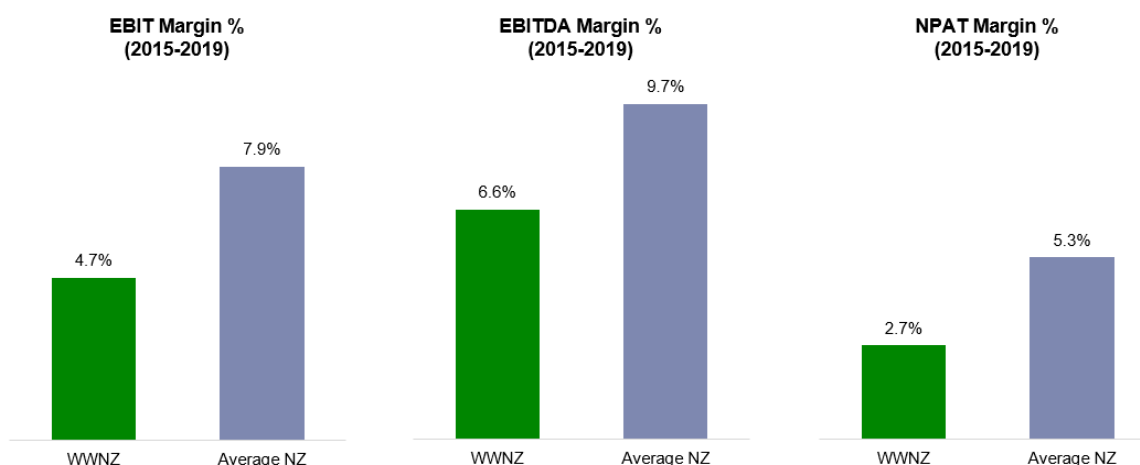
¹⁵⁷ FY2020.

¹⁵⁸ (2019). Bankwest Future of Business: Focus on Supermarkets Report. Retrieved from: <https://www.bankwest.com.au/content/dam/bankwest/documents/business/insights/focus-on-supermarkets-report-2019.pdf>

margins and Returns on Capital Employed than we do.

- 27.4. **Our margins and returns are lower than other large retailers in New Zealand:** While noting the difficulties in comparing between businesses (see Exhibit D10 below), our average EBIT margins (4.7%) are lower than the average (8.1%)¹⁵⁹ of other publicly listed retailers in New Zealand.¹⁶⁰ Similarly, a comparison of the more widely used measure of return, Return on Capital Employed,¹⁶¹ shows WWNZ at 9% achieving significantly lower returns (using the same measure) than other major New Zealand retailers such as Hallensteins Glassons (67.9%), Briscoes Group (44.3%), and The Warehouse (16.1%).¹⁶²

*Exhibit D10: Average EBIT, EBITDA, and NPAT margin by WWNZ and other New Zealand retailers (2015 - 2019)*¹⁶³



- 27.5. **There are issues with the Commission's international grocery retailer comparisons:** There are some issues and errors in the comparisons made between the returns of WWNZ and international grocery retailers, including:

- 27.5.1. Not considering the impacts of accounting write-offs: The Commission's analysis understated the returns of a number of the other international supermarket retailers that it compared to WWNZ because it allowed extraordinary items and accounting write-offs to reduce those retailers' returns. For example, the Commission's analysis allowed Tesco's returns to be reduced by Tesco writing off GBP5.7 billion worth of assets and impairments in 2015, and allowed Empire's returns to be reduced by CA\$3.1 billion of asset write-offs and impairments in 2016. Correcting for such accounting write-offs would materially increase the returns of the supermarkets that the Commission is comparing WWNZ to.

¹⁵⁹ Avg 2016-2019, based on NERA analysis of FactSet financial data for publicly listed NZ retailers.

¹⁶⁰ The average includes Smiths City Group Ltd, The Warehouse Group Ltd, Hallenstein Glassons Holdings Ltd, Briscoe Group Ltd, and Kathmandu Holdings Ltd.

¹⁶¹ These Return on Capital Employed figures are pre-tax, and calculated using a different methodology to that used in the Draft Report.

¹⁶² Three year average. Armillary Private Capital "Return on Capital Employed - Review of 2019 Returns" / Armillary Private Capital "Return on Capital Employed - Review of 2018 Returns."

¹⁶³ The average includes Smiths City Group Ltd, The Warehouse Group Ltd, Hallenstein Glassons Holdings Ltd, Briscoe Group Ltd, and Kathmandu Holdings Ltd.

27.5.2. Not considering different accounting standards and approaches: The accounting policies for many of these businesses vary significantly, which makes any comparison difficult.¹⁶⁴ For example, the gross profit margins in the international sample range from around 4% to over 30%. This very wide range is likely due more to different accounting policies, rather than anything else (such as competitive conditions). For example, we note from the annual accounts of Sainsbury's in the UK that they include store and warehouse costs in their cost of sales,¹⁶⁵ which are costs that are not included in the cost of sales for WWNZ. If WWNZ adopted a similar policy to Sainsbury's then WWNZ's gross profit margin would be less than 10% (instead of 24%). As explained to the Commission in the lead up to the Draft Report, there are many different potential components of gross profit (and accounting choices that can be made in calculating those), and Woolworths Group, including WWNZ, is one of the few supermarket retailers internationally that does not take into account store and warehousing costs in calculating its "gross profit", so WWNZ's gross profit cannot be compared on a "like-for-like" basis with other overseas retailers. Conclusions about competition also cannot be drawn from trends in gross profit given the number of different factors that influence that metric. For example, WWNZ has achieved an increase in gross profit (while its retail prices have been decreasing in real terms) by focusing on efficiencies and implementing innovations, such as reducing stock loss, reducing wastage, improving the mix of products sold, and enhancing efficient use of our DCs.

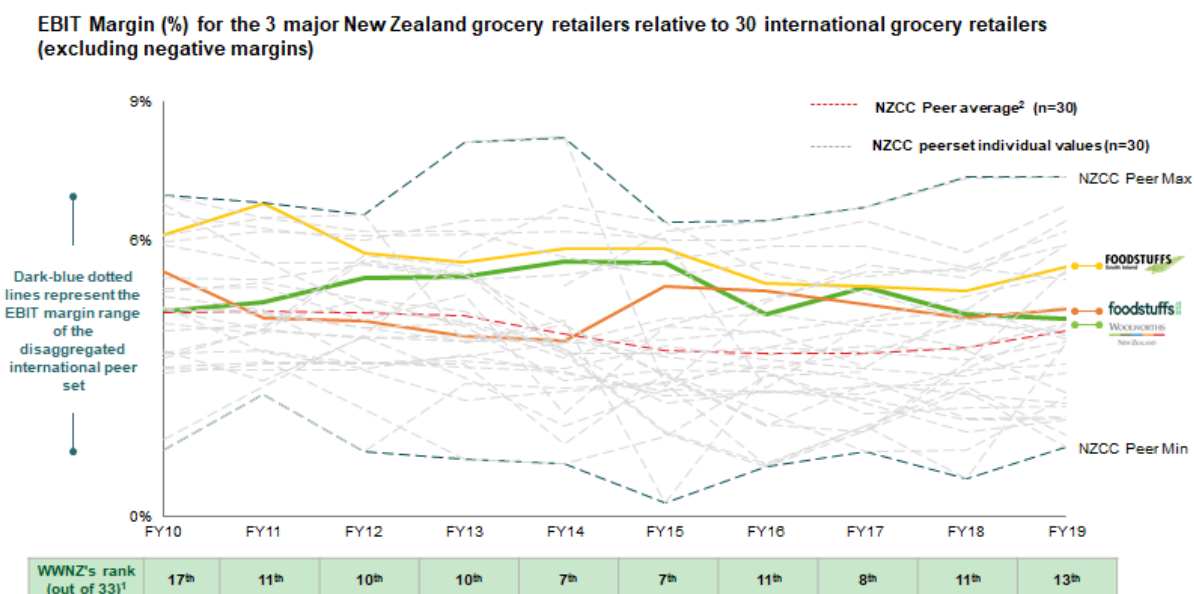
27.5.3. Sample limitations and notable omissions of comparable retailers: The Commission excluded from its comparator set a number of prominent supermarkets with higher or comparable average EBIT margin returns to WWNZ.¹⁶⁶ For example: Lidl (4.4%), Aldi (4.7%), Coles (4.0%), Walmart (4.8%), Costco (3.1%), Publix Super Markets (7.9%), Carrefour (2.8%), ASDA (3.6%), Wal-Mart de México (7.7%), Organización Soriana (5.6%), Metro (5.9%), Esselunga (5.6%), Eroski (2.5%), and ICA Gruppen (4.2%). The average of these excluded retailers is 4.8%, which exceeds the average calculated for WWNZ (4.7%). There were also issues with the retailers the Commission included in its comparison set. For example, the Commission included all of George Westin's operations (including its pharmacy and financial services division), rather than just focusing on its Loblaw retail grocery business (and, therefore, understated its 5-year EBIT margin at 5.1%, instead of 5.7%).

When a comparison to the actual margins of overseas retailers is made by disaggregating their margins, that comparison shows that WWNZ's margins are consistent with other international retailers and is consistent with what is seen in other highly competitive markets. This is shown in Exhibit D11 below, which shows a disaggregated view of the international sample of retailers that the Commission showed an average for in Figure 3.5 of the Draft Report. This exhibit also shows the significant variability and volatility in the comparison sample (highlighting the limitations of such a comparative approach), while also highlighting WWNZ's trending towards the midpoint over the past 5 years.

¹⁶⁴ While the Draft Report stated that the Commission was aware of the limitations of comparing profitability measures between companies [paragraph 3.59], it then proceeded to do so [C225].

¹⁶⁵ J Sainsburys Plc, Annual Report and Financial Statement 2021. Available at: <https://www.about.sainsburys.co.uk/~media/Files/S/Sainsburys/documents/reports-and-presentations/annual-reports/sainsburys-ar2021.pdf>

¹⁶⁶ 5-year average EBIT margins are across 2015-2019, except Lidl (2014-2018), and Aldi (which is a 4-year average due to data limitations).

Exhibit D11: Disaggregation of the Commission's international EBIT peer comparison¹⁶⁷

- 27.6. **The Commission's analysis does not reflect how returns are assessed commercially:** WWNZ returns are reported annually as part of the Woolworths Group Annual Report. The calculations are based on the accounts that are prepared in accordance with mandatory New Zealand and international accounting and reporting standards as part of our obligations as a subsidiary of a listed entity. The [] reported return is an accepted measure of the pre-tax return on the capital in the business. The Commission has its own way of looking at returns (Return on Average Capital Employed, post-tax), but that does not reflect how returns are assessed commercially.
- 27.7. **Even using the Commission's approach, the Commission has materially overstated our returns:** The Commission's analysis significantly overstates our returns as a result of excluding the cost of key assets that we use to run our business - namely leased assets and brand assets.

In relation to leased assets, that approach:

- 27.7.1. Does not reflect economic reality: Leasing in economic terms is an alternative method of financing the purchase of an asset. In this sense, a lease is similar in economic effect to taking on debt to buy an asset, and indeed would be economically equivalent if the lease covered the entire life of an asset. There is no economic reason to treat leased assets differently from other assets in assessing returns.

¹⁶⁷ There are instances in which the total number of companies each year is less than 33 since some companies have no reported financials in select years; 2.Excludes Countdown, FSNI, FSSI; Note: Data from FY10-FY19; Negative returns have been ignored in this visual representation and averages. Commission list of 30 peers are as follows: Woolworths, Colruyt, Weston, Metro, Empire, North West, Casino Guichard, Rallye, Shufersal, Rami Levy, Victory Supermarket, Tiv Taam, La Comer, Ahold Delhaize, Dino Polska, Jeronimo Martins, Axfood, Bim Birlesik, Sok Marketler, Migros, Adese Alisveris, Tesco, Sainsbury, WM Morrison, Kroger, Grocery Outlet, Sprouts Farmers, WEIS, Ingles, Village Super Market; Source: Commission submitted numbers for 30 peers and Countdown, Commission provided graph for FSNI and FSSI EBIT margins.

- 27.7.2. Is inconsistent with international accounting standards:¹⁶⁸ The Draft Report's approach is at odds with international accounting standards. The international accounting standards (specifically IFRS 16) were amended to capitalise leased assets on the basis that would mean the accounting treatment best reflects economic value - for example: *"IFRS 16 will result in a more faithful representation of a company's assets and liabilities and greater transparency about the company's financial leverage and capital employed."*¹⁶⁹ However, the Draft Report states that the Commission has excluded capitalised leased assets on the basis that the Commission is "only interested in the economic value of assets and not accounting standards."¹⁷⁰ That does not make sense to us - especially when the accounting standard was changed to better reflect economic reality. As the enclosed NERA Report states "[t]he change in accounting standard means accounting values more accurately reflect economic value", whereas the Draft Report adopted the opposite approach (that is, prioritising former accounting treatments over true economic value).
- 27.7.3. Is inconsistent with the approach of investors, analysts, and rating agencies: For many years prior to the implementation of the IFRS 16 accounting standard, investors, equity analysts, and rating agencies (including Moody's credit rating methodology) were making adjustments to companies' balance sheets to capitalise the value of leases to obtain a more complete view of the true economic value of the assets (and liabilities) of firms.¹⁷¹ The approach taken in the Draft Report is, therefore, inconsistent with the way in which those investors, analysts, and rating agencies assess economic value.
- 27.7.4. Is inconsistent with the Commission's own approach in its Retail Fuel Market Study: In its Retail Fuel Study the Commission said "[w]e agree there is an arguable case for including the present value of the lease payments within capital employed"¹⁷² and that a firm's market value included "the value of capitalised leases".¹⁷³ However, in the Draft Report the Commission said "we do not consider including the leases in total assets employed is appropriate when assessing economic profit". We see no justification for the Commission to take a different approach in this Market Study.

In relation to brand assets, again that approach:

- 27.7.5. Does not reflect economic reality: There is no economically sound reason for excluding the value of WWNZ's brand assets. Brands are a key asset that supermarket retailers need to invest in to run a successful business. It is incorrect for the Commission to state that a brand asset "does not represent a specific asset that is being employed to generate earnings."¹⁷⁴ Reflecting that, Oxera has observed that brand assets:¹⁷⁵

"are very similar in nature to tangible assets. Investment is made today in the expectation of making a return tomorrow. Therefore, today, investors will expect

¹⁶⁸ IFRS 16.

¹⁶⁹ IASB IFRS 16 "Effects Analysis, at page 5.

¹⁷⁰ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [C76.1].

¹⁷¹ To ignore the impact of IFRS 16 is, in effect, to advocate for off-balance sheet financing and the potential distortionary impact of leases when assessing returns.

¹⁷² Commerce Commission "Market study into the retail fuel sector - Final report" (5 December 2019) at [C234.5].

¹⁷³ Commerce Commission "Market study into the retail fuel sector - Final report" (5 December 2019) at [C66].

¹⁷⁴ Commerce Commission "Market study into the retail fuel sector - Final report" (5 December 2019) at [3.24] and [C69].

¹⁷⁵ Oxera Agenda 2014. Something for nothing? Returns in low-asset industries? Retrieved from: <https://www.oxera.com/insights/agenda/articles/something-for-nothing-returns-in-low-asset-industries/>

returns on investments from previous years. This can be addressed by ‘capitalising’ certain operating costs—for example ... marketing costs could be capitalised into brand-value assets... While they are not ‘assets’ for accounting purposes, these liabilities and assets are otherwise very similar to those for an asset-intensive business—profits in current and future periods will be driven by the level and effectiveness of investments made in prior periods.”

27.7.6. Is inconsistent with the Commission’s own approach in its Retail Fuel Market Study:

In its Retail Fuel Market Study the Commission stated that a “known brand should attract additional customers to the retail sites, regardless of whether it is developed internally or acquired. We therefore include the cost of Z Energy’s 2011 rebrand as one of its intangible assets.”¹⁷⁶ We see no justification for the Commission to take a different approach in this Market Study.

27.7.7. For these reasons, we believe that the Commission’s approach in relation to lease assets and brand assets is fundamentally wrong.

27.7.8. We also do not agree with the Commission’s exclusion of WWNZ’s goodwill asset from its asset base. WWNZ’s goodwill asset is far and away the most valuable asset on our balance sheet. As the Draft Report acknowledges, a goodwill asset will be generated at the time of a business acquisition (as occurred with WWNZ) as the difference “between book value and purchase price” and will occur as a result of “book value undervaluing the assets of the business”.¹⁷⁷ To suggest, as the Draft Report does, that goodwill can be excluded on the basis that it reflects an expectation of future “rents” (from an expected lack of competition) is incorrect and does not reflect commercial reality. Two recent real-life examples illustrate this:

27.7.8.1. Amazon’s acquisition of Whole Foods: Out of the USD 13.2 billion that Amazon paid for Whole Foods in 2017, USD 9 billion (68%) was accounted for as goodwill.¹⁷⁸ Prior to the acquisition, Whole Foods had been reported as “struggling in an intensely competitive environment”.¹⁷⁹ There was no suggestion that the goodwill was in any way attributable to an expected lack of competition.

27.7.8.2. Morrisons sale to Private equity: Morrisons, the fourth largest supermarket chain in the UK, has been subject to a private equity bidding war in the first half of 2021.¹⁸⁰ The current leading acquisition offer is worth GBP 7 billion,¹⁸¹ which is GBP 2.8 billion higher than Morrison’s 2021 net asset book value of GBP 4.2 billion.¹⁸² Being the fourth player in the market makes it unlikely that this premium reflects an expectation that Morrisons is earning market power rents or an expectation of a lack of

¹⁷⁶ Commerce Commission “Market study into the retail fuel sector - Final report” (5 December 2019).

¹⁷⁷ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [3.41].

¹⁷⁸ Amazon.com, Inc. Form 10-K filed with the United States Securities Exchange Commission. File No. 000-22513. Available at:

<https://www.sec.gov/Archives/edgar/data/0001018724/000101872418000005/amzn-20171231x10k.htm>

¹⁷⁹ (November 7 2016). Whole Foods: A Year To Forget. Forbes. Available at:

<https://www.forbes.com/sites/gurufocus/2016/11/07/whole-foods-a-year-to-forget/?sh=55c7fbc62de>

¹⁸⁰ (31 July 2021). Morrisons takeover could trigger breakup, analysts warn. City AM. Available at:

<https://www.cityam.com/morrisons-takeover-could-trigger-breakup-analysts-warn/>

¹⁸¹ (19 August 2021). UK’s Morrisons Agrees To CD&R’s \$9.54B Takeover Offer. Competition Policy International. Retrieved from:

<https://www.competitionpolicyinternational.com/uks-morrisons-agrees-to-cdrs-9-54b-takeover-offer/>

¹⁸² Wm Morrison Supermarkets PLC Annual Report and Financial Statements 2020/21

competition.

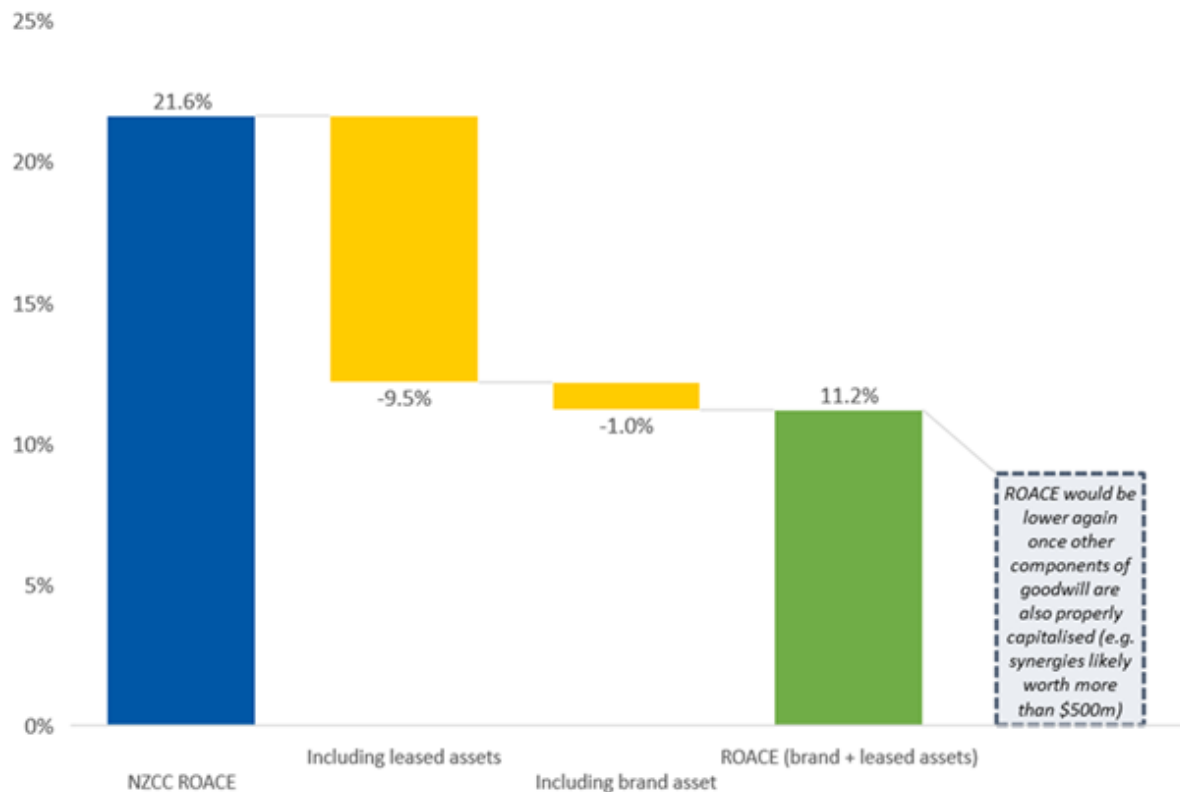
- 27.7.9. This demonstrates that goodwill assets are often generated at the time of a business acquisition in the absence of any expectation of a future lack of competition. To suggest otherwise is fundamentally wrong and is not reflective of commercial reality. It is also inconsistent with the Commission's approach throughout the rest of the Draft Report where it says economic measures are to be preferred over accounting measures¹⁸³ (given, at its core, goodwill is generated as an outcome of accounting whereby the economic value placed on an asset exceeds the accounting book value). As outlined to the Commission during this Market Study, WWNZ considers that the goodwill was generated because book value at the time of Woolworths' acquisition of WWNZ¹⁸⁴ was materially below the true economic value of the business, including because:
- 27.7.9.1. WWNZ's assets were heavily depreciated at the time of the acquisition, well below true replacement value.
 - 27.7.9.2. Land values were recorded on the balance sheet at a historic cost of \$59m, not fair market value.
 - 27.7.9.3. The value of long-term leases was not capitalised at the time.
 - 27.7.9.4. Woolworths expected to generate synergies from the acquisition, which, if capitalised, would account for up to [] in additional value.
 - 27.7.9.5. There were other sources of value in the acquisition, not reflected on the balance sheet - including licences, brands, customer contracts, supplier relationships, and transport contracts / networks.
- 27.7.10. Economic analysis by NERA is consistent with our view (see **enclosed**), as is analysis from third party financial analysts: "The Commission argues goodwill and capitalised leases should be excluded from return calculations, but we disagree, given that they constitute shareholders' capital."¹⁸⁵
- 27.7.11. We ask the Commission to address these issues. This is important, as these issues mean that the Commission's analysis overstates our returns by significant amounts and, therefore, is fundamental to the Commission's findings. Namely, if WWNZ's goodwill asset is also included in our asset base, then our Return on Average Capital Employed would be just 6.4%. Or, even assuming the Commission's exclusion of goodwill is correct (which we also disagree with), exclusion of just the lease assets and brand assets is the difference between our Return on Average Capital Employed being 21.6% (as calculated in the Draft Report) or 11.2% (as calculated if our leased assets and brands are taken into account). See Exhibit D12 below.

¹⁸³ See for example [3.59] of the Draft Report.

¹⁸⁴ Then called Progressive Enterprises Limited.

¹⁸⁵ Jefferies Australia Pty Ltd. Equity Research. 28 July 2021. NZ Grocery Competition Report Suggests Some Draconian Options.

Exhibit D12: Cumulative impact on Return on Average Capital Employed of including brands and leased assets¹⁸⁶



27.8. We do not agree with how the Commission has assessed WACC:

27.8.1. The Commission has estimated that our WACC (post-tax) is 4.6% to 6.1%. However, Woolworths Group has to calculate our WACC for the purposes of internal business planning and making investment decisions, and it is []. Because of the purposes for which it is used, it is important that Woolworths Group calculates it accurately, and they have no incentive to overstate it. In our view, more weight should be placed on Woolworths Group's calculations, than the Commission's estimates. On this point, it is relevant that the Commission specifically acknowledges in the Draft Report that its "estimate of WACC may not necessarily be appropriate for [smaller New Zealand] grocery retailers. We are therefore unable to reach a conclusion about whether they are earning returns above WACC."¹⁸⁷ We see no reason why the Commission considers that its ability to estimate WWNZ's WACC would be any more accurate or appropriate than its ability to estimate WACC for smaller retailers.

27.8.2. We also disagree with the Commission's core thesis that returns in excess of WACC are evidence of a competition issue. To illustrate the point, almost half of all listed and Crown entities in New Zealand achieve returns greater than WACC.¹⁸⁸ While the Commission has its approach, commercially WACC is not a target to benchmark

¹⁸⁶ NERA analysis, Commerce Commission ROACE Model.

¹⁸⁷ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [3.52].

¹⁸⁸ Armillary Private Capital. Return on Capital Employed. Review of 2019 Returns. Armillary Private Capital. Return on Capital Employed. Review of 2018 Returns.

performance, but rather is the minimum rate of return a corporation needs to achieve to attract capital (that is, to compensate owners, creditors, and other capital providers for the risk inherent in the business). Achieve less than this - a company is destroying value, and capital will go elsewhere. We have hundreds of millions of dollars [] of investment underway or planned in the next two years (see section 33 below for further details). A reasonable level of returns are necessary to enable such investments.

27.9. There are also many other factors, in relation to competition, that influence returns:

- 27.9.1. This includes accounting treatment of many different financial measures (including accruals, depreciation charges, intangible assets, asset valuations, write-downs and impairments), the age of assets, and efficiency. For example, an efficient management can substantially increase a firm's profit even though the competitiveness of the market itself remains unchanged, whereas poor management can have the opposite effect. Most notably, the ACCC has recognised that the age of assets, and how they have been depreciated for accounting purposes, is a significant factor in determining the outcome of returns analysis.¹⁸⁹ Accordingly, the ACCC acknowledged concerns raised about the potentially “misleading” nature of returns analysis, such as Return on Funds Employed, and comparisons in its grocery market study.¹⁹⁰

“However, the MSCs [major supermarket chains] submitted that the [calculated returns] for Australian supermarket retailers may be misleading and not comparable to overseas supermarkets. Coles submitted that its lower building ownership compared to many overseas retail grocery retailers would inflate its [returns]. Woolworths submitted that, with a long-standing business, a significant number of assets would be fully depreciated, also inflating its [returns]. The ACCC agrees that care is needed when interpreting [returns analysis] as it is heavily influenced by the value of the underlying assets and the extent of depreciation. Given this, the ACCC considers that significant conclusions cannot be drawn from ROFE...”

The statement in the Draft Report that the ACCC study “did not state why they had not used [returns analysis]”¹⁹¹ is incorrect. As noted above, the ACCC explained why it would not rely on such analysis. This is important for businesses such as supermarkets that often have heavily depreciated assets. We ask that this be addressed in the Final Report.

- 27.9.2. Given WWNZ has a number of long-lived, heavily depreciated assets, this is inevitably a significant driver of the Commission’s calculation of WWNZ’s returns.¹⁹² Indeed, even where there has not been any long-term excessive pricing or profits (for example, cashflows of a business over its life cover the cost of capital and no more), the Commission’s approach to calculating returns will *always* find returns in excess of WACC for a business with long-lived assets that have already been heavily depreciated (such as WWNZ) (See the **enclosed** report by NERA). However, in contrast to the ACCC, the Commission’s Draft Report does not apply such caution. Instead, the Draft Report uses its returns analysis to justify a range of findings, and the canvassing of a range of extreme options. In our view, not only is significant

¹⁸⁹ ACCC. Report of the ACCC inquiry into the competitiveness of retail prices for standard groceries. (July 2008). At page 111.

¹⁹⁰ ACCC. Report of the ACCC inquiry into the competitiveness of retail prices for standard groceries. (July 2008). At page 111.

¹⁹¹ Commerce Commission “Market study into the retail fuel sector - Final report” (5 December 2019) at [C42].

¹⁹² On average between FY2015 to FY2019 WWNZ’s fixed assets were more than [] depreciated, and our Plant & Equipment was more than [] depreciated.

caution required in interpreting returns analysis, but the Commission's approach to returns analysis is fundamentally incorrect (see paragraphs 27.6 and 27.7 above) and predestined, in our view, to find returns that exceed WACC in most industries that it analyses using this approach.

27.9.3. The Commission similarly noted in its retail fuel market study that using accounting information for market study purposes comes with "inherent limitations".¹⁹³

27.10. **We do not agree with the Commission's interpretation of our business cases:** The Draft Report includes a preliminary finding that we have an expectation of excess returns based on a review of our business cases for certain investments that we have made. However, that is not a correct interpretation of those business cases. The problem stems from the fact that the Commission only asked us for business case materials in relation to a certain type of investment - namely, investments in new supermarkets, refurbished / expanded supermarkets, or investments in our online shopping offering. That is of course only a small subset of the investments that we make, and reflects investments in the consumer-facing (that is, revenue-generating) parts of our business (that is, "growth" investments). Investments in such "growth" projects make up only about [] of our capital investment in most years.¹⁹⁴ In any given year there is significant capital expenditure on items that are referred to as "stay in business" expenditure, and a large proportion of that is not expected to make any material return.¹⁹⁵ Examples include seismic strengthening of buildings, replacement of store or warehouse equipment, IT systems and hardware replacements, and investments in health and safety initiatives for our people.¹⁹⁶ Of course, we cannot have the consumer-facing part of our business without those important "stay in business" investments, but they do not generate returns themselves. It is not appropriate to only assess individual business cases for "growth" investments, as "growth" business cases need to achieve returns above cost of capital to enable the business (on a total basis) to at a minimum achieve its WACC. As a result, the financial return across WWNZ's total capital expenditure will be significantly lower than the range referred to in the Draft Report. The approach in the Draft Report is artificially narrow - it excludes two thirds of our investments (FY2020). Therefore, it cannot be used to reach conclusions about the expected returns of a business as a whole. Again, we regard this as a fundamental point.

27.11. **In summary,** our view is that in a number of ways the Draft Report has overstated our returns - both in absolute terms and in comparison to other retailers overseas. We do not consider that the Commission's analysis can be relied upon as evidence of a competition issue, or that our returns are excessive. We reiterate that even if our profit was zero (an unsustainable position), New Zealand's price ranking (based on the Commission's view) would not change relative to the rest of the world.¹⁹⁷

¹⁹³ Commerce Commission "Market study into the retail fuel sector - Final report" (5 December 2019) at [C180] to [C181].

¹⁹⁴ Even in respect of this subset of investments in stores, we explained to the Commission in our responses to information requests that [] and so will overstate any potential returns [].

¹⁹⁵ The way we approach capital investment is to (a) reinvest to sustain the business (that is, "stay in business" expenditure), which is largely low or minimal returning spend, and (b) invest a portion of capital expenditure on "growth" initiatives, which is required to achieve growth and to offset cost inflation.

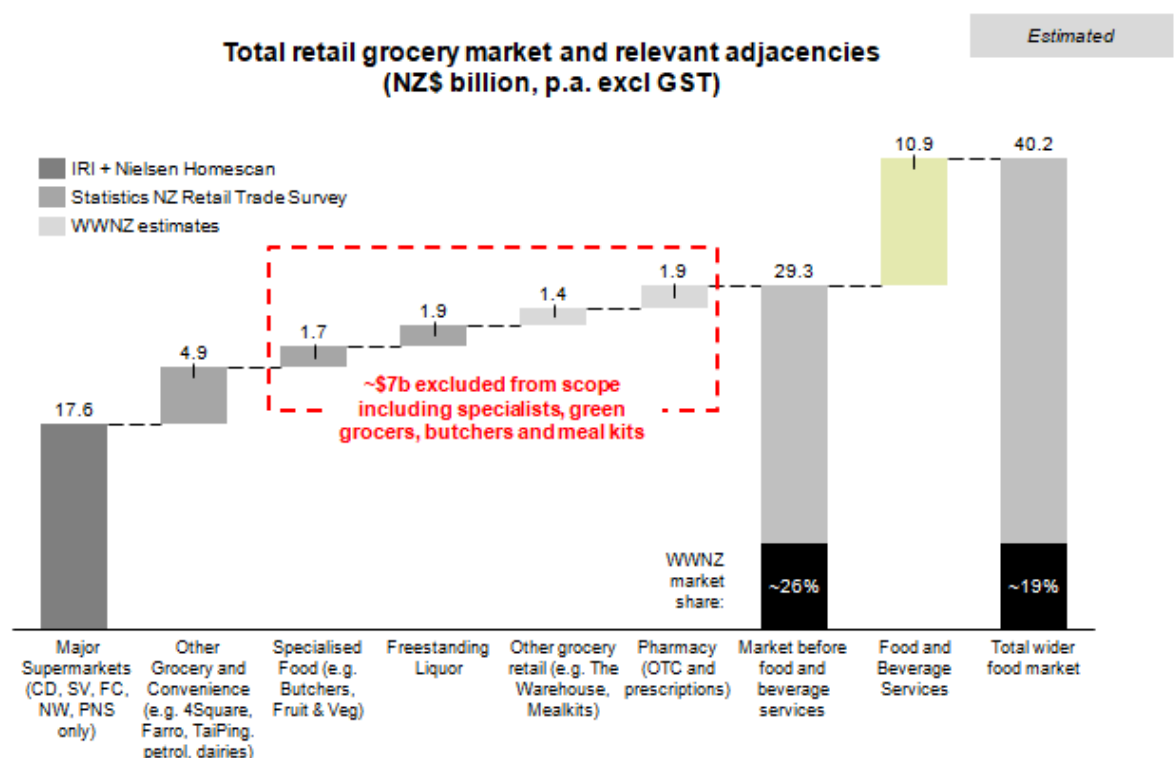
¹⁹⁶ For example, WWNZ is making significant investments across its transport and logistics fleet to enhance safety of goods loading zones in its stores.

¹⁹⁷ Analysis by WWNZ and NERA Economic Consulting.

28. Despite the Draft Report's narrow framing of the market, the New Zealand retail grocery sector is intensely competitive, and new entry is inevitable

28.1. As discussed in our Initial Submission “the total New Zealand food and grocery market is worth \$29 billion annually, or \$40 billion including wider food and beverage services adjacencies”. Consistent with WWNZ’s view, My Food Bag also talks about operating in “the \$37 billion New Zealand retail food sector”.¹⁹⁸ The Draft Report’s narrow focus on WWNZ, FSNI, and FSSI misses a number of the key dynamics that drive competitive outcomes in our industry. The Draft Report defines the market in its narrowest possible sense at \$22 billion. We outline this in Exhibit D13 below.

Exhibit D13: Total retail grocery market and relevant adjacencies (NZ\$ billion, per annum excluding GST)



28.2. This narrow view of the market understates the importance of a number of competitors including online supermarkets, specialised food providers (for example, butchers, greengrocers and fishmongers), meal kits, liquor stores and other grocery providers. These players play substantial and growing roles in both the main shop and fast increasing non-main shop missions and therefore compete intensely with the major retailers.

28.3. The Draft Report excludes almost half of grocery sales from its frame of reference:

28.3.1. The Draft Report’s focus on “main shop” (and the corresponding lack of consideration of other) shopping trips is outdated with “non-main shop” shopping missions (or “on demand” shopping missions) a critical and increasing area of grocery market competition. In July 2021 “main shop” missions accounted for only 35% of grocery

¹⁹⁸ (6 August 2021). My Food Bag Unveils Kitchen Secrets With Launch Into New Category. Press Release: My Food Bag. Retrieved from: <https://www.scoop.co.nz/stories/BU2108/S00146/my-food-bag-unveils-kitchen-secrets-with-launch-into-new-category.htm>

shopping trips in New Zealand (representing 56% of sales). That means that almost two-thirds of all missions (and almost half of all expenditure), relate to “non-main” shops (for example, customers making purchases without the level of pre-planning that has traditionally gone into a main shop). These are shopping trips the Draft Report does not regard as relevant. See Exhibits D14 and D15 below.

Exhibit D14: Consumer expenditure by different grocery shopping mission type (%)

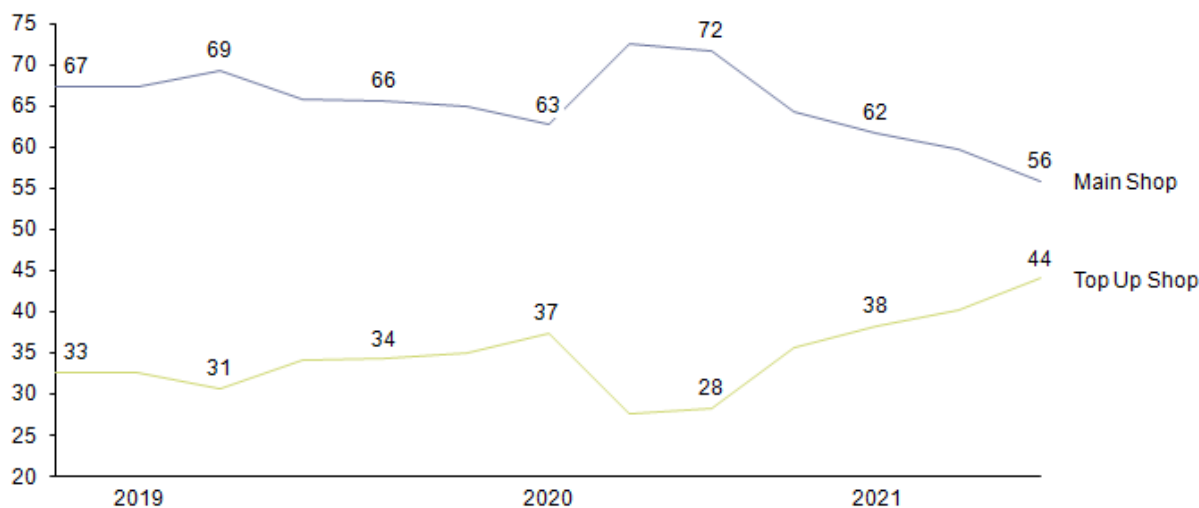
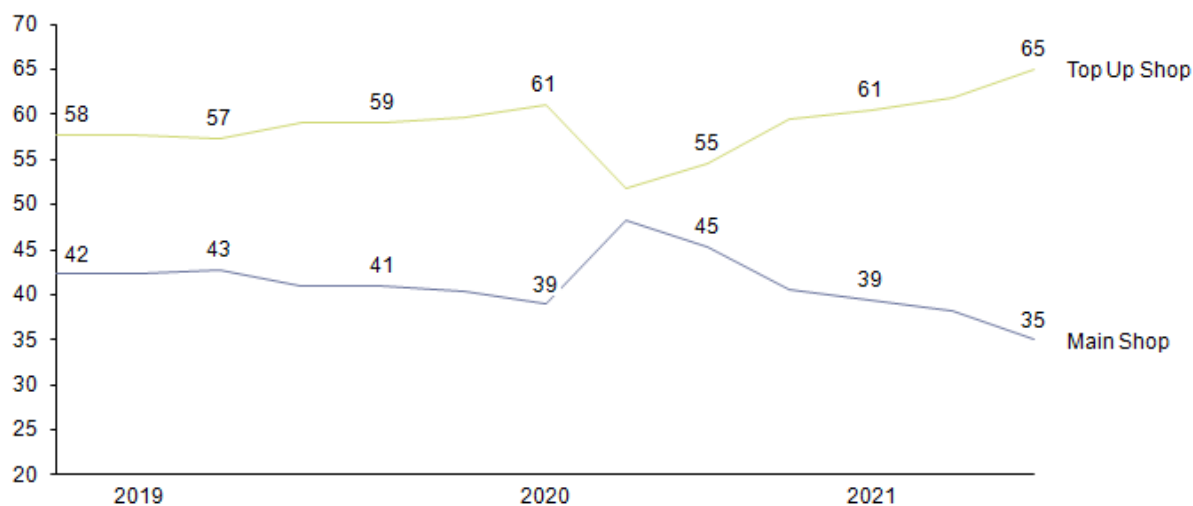


Exhibit D15: Consumer shopping trips by grocery shopping mission type (%)



28.4. Focusing on the main shop ignores the fact New Zealanders are increasingly top up shopping (or on-demand shopping) and the main shop is in decline:

28.4.1. The relevance of the ‘main shop’ to New Zealanders continues to decline as people look for more convenient options (as per Exhibits D14 and D15 above).

- 28.4.2. Over the past 3 years, expenditure on main shops has fallen from 67% to 56% (a decline of 11 percentage points) while main shop shopping missions have fallen from 42% to 35% (a decline of 7 percentage points).¹⁹⁹
- 28.4.3. As outlined in our Initial Submission, this convenience trend is leading to significant changes in Kiwis' shopping behaviour:
- 28.4.3.1. shoppers are undertaking frequent, shorter in-store trips, versus large weekly shopping trips;
 - 28.4.3.2. there is increasing consumer demand for ready-made meals;
 - 28.4.3.3. consumer expenditure on eating out and takeaway food is growing; and
 - 28.4.3.4. whereas many years ago grocery retail shopping in New Zealand might have been a once-a-week-or-fortnight "single large basket" shopping trip, the average Countdown shopper's checkout basket is [] (including GST),²⁰⁰ and approximately [] items, with the average Onecard holder now visiting us [] times per week.²⁰¹
- 28.4.4. In response, there has been substantial investment made by New Zealand grocery retailers to cater for changing customer needs. We have launched our Metro format and we are in the process of building a neighbourhood Metro store in Herne Bay. Additionally, FSNI has launched its New World Fresh Collective, New World Metro, and PAK'nSAVE Mini formats while Farro Fresh has now established six of its smaller format grocery stores, and Circle K has expanded into New Zealand.
- 28.4.5. This trend is consistent with what we have seen globally as retailers move towards smaller, more convenient stores, and other on-demand innovations.
- 28.4.5.1. For example, in the UK, a number of supermarkets (for example, Aldi, Tesco, Sainsbury's) have been investing in the development and expansion of smaller-format grocery stores.
 - 28.4.5.2. In Europe, America and Australia, a number of grocery retailers have been introducing on-demand solutions and services (e.g, delivery subscriptions, online same-day and express options).
 - 28.4.5.3. In Australia, both Woolworths and Coles have been scaling up their Metro and Local (respectively) store networks, and Aldi has now launched a small format offering - noting: "The Aldi Corner Store was commissioned by Australia for Australia, but local smaller formats are becoming increasingly important globally".²⁰²

Therefore, a focus just on "main shop" in the grocery market is only partially representative of how customers currently shop, and of how we compete, and will become even less representative over the coming years as the prominence of "top-up" and "on-demand" shops continues to increase.

¹⁹⁹ [].

²⁰⁰ [].

²⁰¹ Excluding some temporary COVID-19 disruption during the panic buying / stock-up period.

²⁰² (16 July 2021). Aldi Debuts Small-Format 'Corner Store'. Progressive Grocer. Available at: <https://progressivegrocer.com/aldi-debuts-small-format-corner-store>.

28.5. The Draft Report excludes online grocery retailers:

- 28.5.1. The Draft Report's focus on "bricks-and-mortar" retailers, to the exclusion of online grocery sales, does not capture the full competitive landscape or take a forward-looking view (as the Commission does in conducting merger analysis in order to accurately assess competitive dynamics²⁰³ and as has been described by the OECD as a key strength of market studies).²⁰⁴ See further at paragraph 28.6 below.
- 28.5.2. Countdown's online penetration continues to rapidly grow, having increased from 3% of total sales in FY2014 to over 12% in FY2021, and []²⁰⁵ (that is, an increase of over 400% [] from FY2014 to FY2021).²⁰⁶ This means that the size of Countdown's current online business is already equivalent to over 20 physical supermarkets, and by the end of FY2023 would be as large as more than [] supermarkets. This is plainly where a significant and ever-increasing number of Kiwi consumers are choosing to purchase their groceries. Excluding online retailers ignores that online retailing will increasingly become the key area of competition and will provide opportunities for new businesses and innovative business models.

28.6. The Draft Report does not factor in recent developments or forward looking trends:

- 28.6.1. In our view, the Draft Report did not take a forward looking view of the nature of competition in the retail grocery market. This means that it misses a number of key emerging trends. To best understand the competitive dynamics, and identify options that are fit for purpose, it is important that the Commission's Final Report factor in recent developments and take a forward looking approach (as has been described by the OECD as a key strength of market studies).²⁰⁷ In particular, it is important for the Final Report's findings to reflect that the retail grocery industry, like many other industries, is changing rapidly. In the last year alone, New Zealand has seen UberEats launch a grocery delivery offering (see Exhibit D16 below),²⁰⁸ My Food Bag expand into online delivery of grocery products (beyond just meal-kits, see paragraph 30.2.3), and new online grocers like The Honest Grocer and Supie launch.

²⁰³ "The analysis is a forward-looking one, comparing the likely state of competition if the merger or acquisition proceeds with the likely state of competition if it does not." *New Zealand Bus Ltd v Commerce Commission* [2007] NZCA 502 at [237]. See also Commerce Commission "Mergers and acquisitions guidelines" (July 2019) at [2.35], in which the Commission notes that it takes a "pragmatic and commercial assessment of what is likely to occur in the future with and without the merger".

²⁰⁴ OECD (2020). Using market studies to tackle emerging competition issues. www.oecd.org/daf/competition/using-market-studies-to-tackle-emerging-competitionissues-2020.pdf

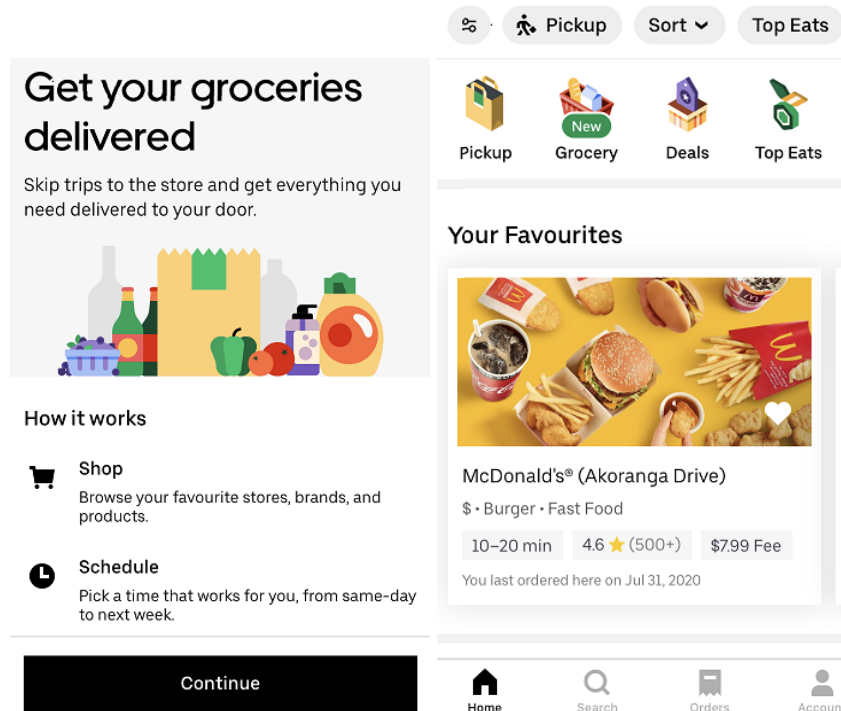
²⁰⁵ Measured prior to the latest August 2021 Level 4 lockdown.

²⁰⁶ In our view, the fact that our online penetration has grown from 12% at the time of our Initial Submission to [] by July 2021 (measured prior to the latest August 2021 Level 4 lockdown), further reinforces that it is incorrect for the Draft Report to state that New Zealand has "slow growth of online grocery sales" (at [5.69]) / "relatively low penetration and growth of online sales" (at [6.121]).

²⁰⁷ OECD (2020). Using market studies to tackle emerging competition issues. www.oecd.org/daf/competition/using-market-studies-to-tackle-emerging-competitionissues-2020.pdf

²⁰⁸ (8 October 2020). Uber Eats to deliver groceries, medication, flowers in new update. Stuff. Retrieved from: <https://www.stuff.co.nz/business/122995019/uber-eats-to-deliver-groceries-medication-flowers-in-new-update>

Exhibit D16: Screenshots from the UberEats (New Zealand) App relating to its grocery delivery offering



28.6.2. These developments in New Zealand are manifestations of the key trends that are emerging in grocery retailing internationally.²⁰⁹ For example, in a paper seeking to identify the key “trends we expect to shape the grocery retail market in the coming years”, McKinsey cited the following:²¹⁰

28.6.2.1. “The shift to online is likely to have some of the most pronounced implications over the coming years... For grocers, winning market share without winning online will become increasingly difficult... Many retailers are currently investing in their online business to gain a larger share of customers’ wallets and stomachs. In this game, they are up against pure

²⁰⁹ As mentioned in our Initial Submission, internationally there are any number of significant technology and business model disruptions underway, at scale. Some of the major players include:

- Ocado, a dedicated online grocer and notable offshore example (valued at >GBP21.7 billion) plays a significant role in the UK grocery market and is steadily expanding its influence globally (for example, in the US - via Kroger, in Australia - via partnership with Coles).
- Amazon, the world’s largest online retailer acquired Wholefoods in 2017 and has been steadily building scale in online grocery right across the globe, both in pantry staples and fresh. In Australia, Amazon launched its food and grocery offer in 2018.
- Disintermediation models are also gaining traction around the world and can be expected to impact New Zealand in the near future. In Europe, for example, tech company INS has developed a digital platform allowing food manufacturers to bypass the brick-and-mortar retail landscape and sell their products directly to their consumers.
- In North America, Instacart (valued at >US\$17 billion), operates a grocery delivery and pick-up service in the United States and Canada, offering its services via a website and mobile app and allowing customers to order groceries from participating retailers with the shopping being done by a personal shopper. Notably, Instacart is already partnering with Costco in these markets.

²¹⁰ Disruption & Uncertainty. The State of Grocery Retail 2021. Europe. McKinsey & Company. Retrieved from: <https://www.mckinsey.com/~media/mckinsey/industries/retail/our%20insights/the%20path%20forward%20for%20European%20grocery%20retailers/disruption-and-uncertainty-the-state-of-grocery-retail-2021-europe-final.pdf>

online competition, as well as against alternative business models, such as meal-kit providers and meal-delivery platforms — business models that are often much more highly valued by investors due to their high growth expectations.”

28.6.2.2. “Formats with distinct value propositions, such as prepared-food delivery, discounters, convenience stores, and online stores, are leaping ahead and taking market share from traditional supermarkets... Consumers are emphasizing more convenience, such as food delivery and more ready-to-eat food.”

28.6.2.3. “The supermarket is threatened as alternative formats cater to a more fragmented customer landscape.”

28.6.2.4. “Innovative digital players continue taking share from offline stores—mainly supermarkets and hypermarkets—as they compete on price, assortment, and ultra-convenience through features such as home delivery of groceries and nonfood items.”

28.6.2.5. “Convenience stores have also made a comeback in recent years, offering a highly targeted assortment in a small format of less than 400 square meters.”

28.6.2.6. “Many online giants [such as Amazon and Alibaba] have added grocery to their ecosystems and are using customer data from across their offerings—such as nonfood, payments, and social media—for optimization purposes. For these players, their grocery divisions do not necessarily need to be profitable as stand-alone businesses; instead, the grocery operation supports the overall profitability of the ecosystem by securing daily traffic and engagement on the platform, thereby boosting loyalty and customer lifetime value and allowing for different, new revenue models, such as media monetization.”

28.6.3. From our perspective, the Draft Report did not take these key emerging trends and dynamics into account in reaching its preliminary findings, nor in the options that it canvassed. We ask that the Final Report apply a forward looking lens to ensure it does not miss key aspects of both current and emerging competitive dynamics, and to best ensure any options that are canvassed are fit for purpose. In particular, our perspective is that these changes to competitive dynamics, including the range of likely new entrants and emerging business models, reinforce our view that the market is intensely competitive, and that no significant or novel regulatory intervention would be required (and that the risk of detriments to consumers, and unintended consequences, from such intervention is exacerbated given new competition will inevitably emerge, and legacy retailers will increasingly need to innovate to remain competitive with those emerging competitors).

28.7. The consumer survey the Commission used to define its frame of reference as the “main shop” has significant limitations:

- 28.7.1. In our view, the consumer survey that the Commission used to draw conclusions about competition has significant limitations.²¹¹
- 28.7.2. In particular, the Commission used consumers' perceptions, as reported through the survey, as evidence of an issue with main shop competition - even where those reported perceptions were inconsistent with actual dynamics.
- 28.7.3. For example:
- 28.7.3.1. Consumers reported a perception that product range was reducing. That is not correct. Countdown offers 26,000 products, similar to the number of products we offered five years ago.
- 28.7.3.2. Consumers reported a perception that prices had increased relative to their income. This is not correct. Over the last decade food expenditure in New Zealand has decreased as a share of household income (from 12.5% in 2010 to 11.5% in 2019). When restaurant meals and 'ready-to-eat' food expenditure is excluded, this decrease is even larger - from 9.5% in 2010 to 8.1% in 2019.²¹² This means that today a smaller portion of households' income is being spent on retail grocery food than 10 years ago (despite the cost pressures on retailers).
- 28.7.3.3. Consumers reported a perception that "limited competition" was driving higher prices, yet WWNZ makes lower margins than Woolworths Australia (see paragraph 27.2 above), with Australia regarded as "highly competitive".
- 28.7.4. That the perceptions reported to the Commission through the survey do not reflect the evidence is, in our view, a result of a number of methodological flaws in the Commission's survey as well as the general challenges of perception versus reality. The manner in which the Commission has then relied on those perceptions also reflects that the Draft Report more generally appeared to place undue weight on anecdotal perception rather than data evidence. Namely, the Commission noted that consumer perception is "perception only" and not "evidence that prices are in fact higher than we might expect", however, it then proceeded to state perceptions "provide[s] us with a view of consumers' confidence in the effect of competition in the market".²¹³ Accordingly, our read of the Draft Report was that the Commission acknowledged the problems with relying on perceptions (rather than evidence) in trying to diagnose whether there is a competition issue, but then chose to rely on perceptions (rather than evidence) in any event in drawing certain conclusions. We do not consider that is a robust way to draw findings in a market study such as this.

²¹¹ In our view there were a number of limitations in the way the survey was designed that did not reflect best practice surveying methodology and, therefore, likely significantly affected the results. At a high-level, those issues include (but are not limited to):

- sampling limitations and potential bias due to using a voluntary online submission methodology (no controlled quota system was used to ensure that the respondent pool was statistically representative); and
- limitations in the survey design including the use of cognitively challenging or hypothetical questions where consumers are unlikely to be able to respond accurately, and unclear wording.

We would be happy to outline these points in more detail if the Commission intends to rely on survey results in its Final Report.

²¹² NERA analysis of Statistics NZ Household Economic Survey (HES) and Labour Force Survey (LFS).

²¹³ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [3.75].

28.7.5. The survey overstates the importance of the “main shop” to Kiwi consumers. This is because the distribution of respondents to the consumer survey skews substantially to older age groups.²¹⁴ For example:

28.7.5.1. 16 to 25 year olds account for ~15% of New Zealand's population aged 16 or over, while they make up ~1% to 2% of respondents to the Commission's survey.

28.7.5.2. 25 to 40 year olds account for ~28% of New Zealand's population aged 16 or over, while they make up ~15% of respondents to the survey.

28.7.6. It is recognised that younger demographics are more likely to undertake smaller, more frequent shopping trips than older demographics. For example, [] data suggests 18 to 44 year adult households with no children spend a smaller proportion of their grocery budget on main shops relative to all family lifecycle groups.²¹⁵ Further, the average basket size of “Young Singles and Couples” who shop at Countdown is only ~67% that of overall shoppers.

28.7.7. The survey overstates the proportion of “main shops” that take place in major retailers. In particular, respondents of Chinese and Indian ethnicity were underrepresented in the survey,²¹⁶ yet the Draft Report notes that international food stores and other supermarkets “are most likely to provide an alternative option to some consumers for their main shop”. Given many international food stores specialise in Chinese and Indian cuisine, we expect the survey results have understated the number of Kiwis who use international food stores as their main shop. This may be even more pronounced for some major centres (for example, Auckland).

28.8. Accordingly, our view is that the Commission's survey is of little value in drawing conclusions about the level of competition in the New Zealand grocery market given its significant reliance on perceptions rather than evidence.

29. Even within the narrowly framed market, competition is strong including on price

29.1. The view in the Draft Report that “existing competition between grocery retailers is weak” is not correct.²¹⁷ A number of points demonstrate this.

29.2. Kiwi consumers switch between a range of different grocery retailers:

29.2.1. As outlined in our Initial Submission, more than half [] of New Zealanders will shop at speciality grocers and non-supermarkets for grocery retail products in a given month, and if we just look at Kiwis who shop at Countdown, PAK'nSAVE, and New World, more than half [] will “cross shop” (meaning they will shop at more than one of these banners) in a given month (Exhibit D17 below). Therefore, the suggestion that WWNZ and FSNI / FSSI attempt to position themselves differently in the market to avoid competition and attract “a more loyal and exclusive customer base” does not reflect market dynamics.²¹⁸ The market dynamics demonstrate that there is no such thing as a “loyal or exclusive customer base” - there is intense and ongoing

²¹⁴ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021), figure F6.

²¹⁵ [].

²¹⁶ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021), figure F5.

²¹⁷ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [5.133].

²¹⁸ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [5.110].

competition between WWNZ, FSNI, and FSSI banners for the same customers. This is demonstrated in the significant extent of cross-shopping by consumers across banners so each supermarket operator needs to compete vigorously to encourage as much of that shopping as possible to be in their stores.

Exhibit D17: Cross-shopping by New Zealand consumers

[]

29.2.2. Analysis []²¹⁹ found that consumers spent [] on food and grocery products at other retailers within 30 minutes either side of a shopping trip to Countdown (where the average shopping basket at Countdown is itself []).²²⁰ This means that even on the same shopping trip, consumers will visit other food and grocery retailers. While respondents to a survey may say they are predominantly in the habit of a weekly main shop, Kiwis' shopping patterns show otherwise.

29.2.3. While shopping, Kiwis are able to compare the attributes of the stores they visit and use this information to decide where to shop in the future. Therefore, supermarkets are competing with all grocery retailers on attributes such as convenience, price, product, quality and store environment for the ongoing custom of New Zealand grocery shoppers. Such high levels of cross-shopping is evidence of vigorous competition between retailers.

29.3. Major retailers compete head to head on a range of price and non price dimensions:

29.3.1. New Zealand has intense price competition - and potentially the highest penetration of any food discount / no frills supermarket anywhere in the world: The Draft Report reaches a view that "price competition between the major grocery retailers is considerably less than we expect to see in a workably competitive market".²²¹ However, that is not supported by the evidence. There is significant price competition in market - and significant evidence of this, including:

²¹⁹ [].

²²⁰ [].

²²¹ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [5.115].

- 29.3.1.1. The fact that retail grocery food prices have fallen in real terms over the last decade (while input costs have increased). See paragraph 26.1 above.
- 29.3.1.2. The Draft Report's finding that there is no evidence that major retailers increase prices at around the same time even though supplier cost increases flow through at similar times.²²²
- 29.3.1.3. The fact that New Zealand already has potentially the highest penetration of any food discount / no frills supermarket anywhere in the world. The Draft Report's suggestion that innovation in the New Zealand grocery sector is not directed at price and that "food discounter type business model innovations such as those offered by Aldi overseas... have not occurred in New Zealand" is incorrect.²²³ Such statements in the Draft report are based on the assumption that there are no "food discounter... no-frills" competitors operating in New Zealand. However, if it were operating in overseas markets, PAK'nSAVE outlets (with their unlined interiors, concrete floors, cardboard boxes in the retail area, and customers asked to pack their own bags), would be classified as exactly that type of competitor.²²⁴ Because PAK'nSAVE has made this its model, it means that to remain competitive we not only need to compete intensely on price, but that we need to stand for more than just price.
- 29.3.1.4. We also note the Draft Report uses a "lack of evidence that entry by two new Farro Fresh stores in Auckland constrained the pricing of the major grocery retailers in close proximity to these new openings" as evidence of other grocery retailers having a limited effect on the prices set by the major grocery retailers. That statement does not reflect how Farro Fresh seeks to compete. Farro Fresh offers a premium shopping experience through "the very best and finest of New Zealand food".²²⁵ Customers attracted to this offer choose it because of the premium nature of the shopping experience. Therefore, the best competitive response for a competitor to win-back (or not lose) those customers would be to enhance its own premium shopping experience (by definition those customers are focused on elements of the price / quality / service equation other than lowest prices). WWNZ competes in this way - for example, having recently upgraded our Richmond Rd Countdown in Grey Lynn which is across the road from a Farro Fresh store.
- 29.3.2. Intense competition on non-price dimensions: In addition to intense price competition, there is also intense competition on other aspects of the supermarket offer - such as convenience, location, quality, ambience and service:
- 29.3.2.1. As outlined in the Draft Report,²²⁶ convenience is a key determinant of store choice, while familiarity with store, service, choice of products,

²²² Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [E41].

²²³ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [3.145].

²²⁴ (10 August 2015) Pak'n Save hits a milestone birthday. Retail NZ. Noting that PAK'nSAVE was founded as "a chain of discount grocery stores, which had a warehouse club feel, with customers bagging their own groceries and an overall no-frills shopping experience". See:

<https://theregister.co.nz/2015/08/10/pakn-save-hits-milestone-birthday/>

²²⁵ About Farro. Retrieved from: <https://www.farro.co.nz/our-story/>

²²⁶ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) figure 4.3.

quality products and pleasant store environment are also key drivers. Therefore, it makes sense for major grocery retailers to compete on both price and non-price dimensions. If all major retailers were to structure their businesses to only focus on price dimensions (that is, to achieve the lowest cost of doing business, but in “no-frills” stores in inconvenient locations), then the market would only be serving the needs of a subset of New Zealand consumers (or if it were the case that perceptions of “lowest prices” was the only thing that mattered to consumers, then consumers would only shop at PAK’nSAVE’s “no frills” stores, but plainly many consumers want more than that).²²⁷

29.3.2.2. We note that the Draft Report was unclear and inconsistent in its explanation of the Commission’s views on the extent of non price competition in the sector.²²⁸ In particular, at some points the Draft Report states that the level of “product and service differentiation” is modest in New Zealand,²²⁹ whereas in other parts the Draft Report states that in New Zealand the major retailers are “focussed on product and service differentiation”²³⁰ and, therefore, “a significant emphasis is placed on growing market share through improving the quality of service, enhancing the overall shopping experience, managing stock levels, increasing product range and ensuring consistency in service levels across all stores.”²³¹ Our view is that the extent to which grocery retailers in New Zealand seek to differentiate their product and service offering through competing on aspects such as innovation, shopping experience, product range and service levels is evidence of the intensely competitive nature of the sector in New Zealand.²³²

30. New retail entry has occurred across both main and non-main shops, and the possibility of further entry and expansion is real

30.1. The Draft Report says that there has not been any new entry in grocery retailing in New Zealand and that this suggests there is unlikely to be further new entry.²³³ We consider that statement to be incorrect on both fronts.

30.2. As the Draft Report notes “[t]here are many different types of grocery retailers operating across New Zealand”,²³⁴ and that includes a number that have entered in the last few years,²³⁵

²²⁷ As the Draft Report notes:

- at [2.5]: “New Zealanders are a diverse group with different wants, needs, and demographics”;
- at [4.23]: “In a workably competitive market, we would expect firms to compete to satisfy this diverse range of preferences. Differentiation on the retail grocery offer may therefore offer benefits to consumers through an expanded set of choices and increased competition between grocery retailers.”

²²⁸ Other inconsistencies include the Draft Report stating (at [4.25]) that “in a workably competitive market, we would expect to see a greater level of differentiation”, but (at [5.110]) that the major grocery retailers “attempt to position themselves differently in the market by differentiating their retail grocery offer on both price and non-price dimensions of the retail grocery offer”.

²²⁹ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at page 35.

²³⁰ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [3.142].

²³¹ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [4.58] and [5.45].

²³² We outline an extensive list of non price innovations that WWNZ has implemented in section 33 in Part D.

²³³ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [6.25].

²³⁴ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [2.8].

²³⁵ As noted at [6.27] of the Draft Report.

including:²³⁶

30.2.1. Farro Fresh, which has six retail stores across Auckland, an online shopping service,²³⁷ 300 staff, and revenue in excess of \$100 million.²³⁸ Farro Fresh's founder has stated: "We still believe there is opportunity for four to five more stores in Auckland of varying sizes – we've got the smaller Mt Eden store which is a real local store – we know how we can make that work well, it's profitable, but we also have the mega store like Grey Lynn or Constellation Drive, which are large format and 70 carparks." While it is currently Auckland focussed in terms of its "bricks-and-mortar" presence, Farro Fresh continues to expand, and:²³⁹

30.2.1.1. is said to be "keeping a South Island move on its radar", first through a "flagship store" and then "expanding into the surrounding areas"; and

30.2.1.2. has launched a new online ordering system that will "now be able to deliver to more customers in Auckland, but also nearby centres such as Hamilton, Rotorua, Tauranga and Mount Maunganui."

30.2.2. Moore Wilson's, which is both a grocery wholesaler and retailer with three retail stores in Wellington, Porirua, and Masterton, including a newly redeveloped Masterton store.²⁴⁰

30.2.3. My Food Bag, which stated in its Product Disclosure Statement that "[w]e regularly review our bags to ensure we are priced competitively to supermarkets" and that its "Bargain Box recipes are designed to be consistently priced below supermarkets (for the equivalent quality ingredients) on a delivered, per portion basis, providing the best value for money option of its kind."²⁴¹ My Food Bag has expanded from just being a meal kit supplier to supplying a range of grocery products as an online grocery retailer through its "Kitchen" offering, which My Food Bag's CEO says is expected to "tak[e] a greater share of New Zealand's substantial grocery spend"²⁴² ("[n]ew products include pantry staples, baking mixes, dessert kits, healthy breakfasts and sides, as well as gourmet local cheeses, meats and ready-made meals, including My Food Bag's own sauces and spices". My Food Bag has announced to its investors that its growth

²³⁶ In addition to the following, we note the Draft Report said there was "planned expansion by other grocery retailers" (at [6.27.6]), but the details relating to that were redacted.

²³⁷ (27 January 2021). Three new Farro Fresh stores planned, \$100m revenue forecast to be topped this year. NZ Herald.

²³⁸ (12 April 2018). Workers of Huckleberry grocery store pack up strike action following pay negotiations. NZ Herald. Retrieved from:

<https://www.nzherald.co.nz/business/workers-of-huckleberry-grocery-store-pack-up-strike-action-following-pay-negotiations/Q6VSZUMARE7E3UV43GMOV2Y4CI/>

²³⁹ (9 July 2021). Farro Fresh expands IRL and online. FoodTicker. Retrieved from:

<https://www.foodticker.co.nz/farro-fresh-expands-irl-and-online/>

²⁴⁰ (18 June 2021). Fresh new store for Moore Wilson's in Masterton. FMCG Business. Retrieved from:

<https://www.fmcgbusiness.co.nz/fresh-new-store-for-moore-wilsons-in-masterton/>

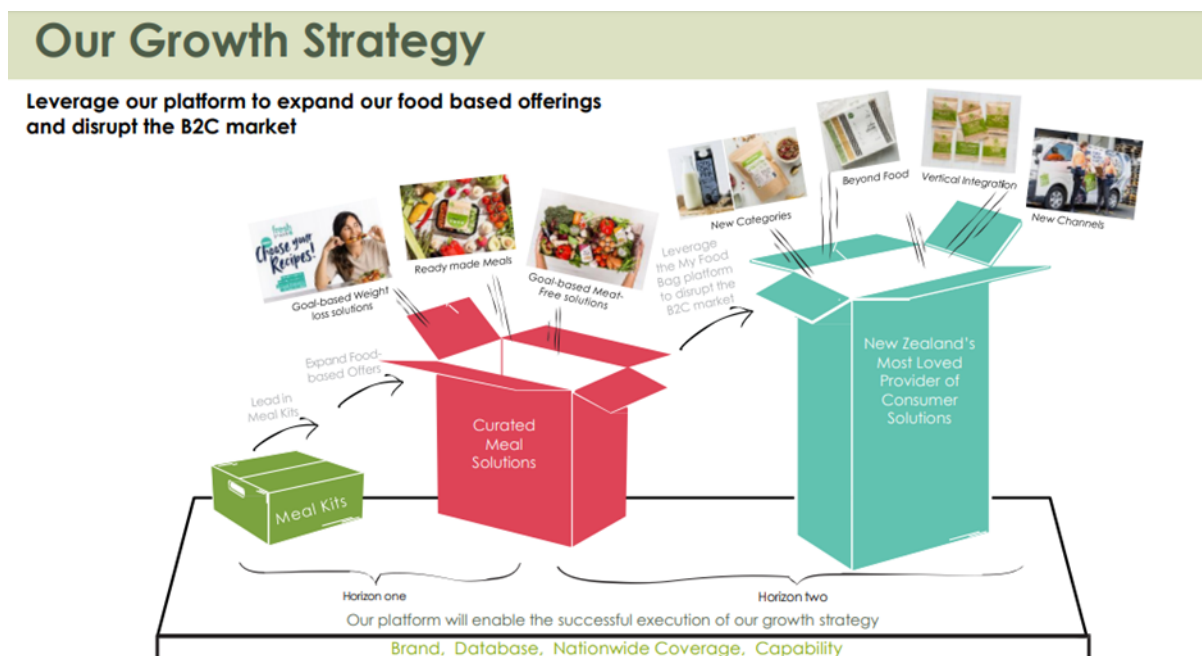
²⁴¹ (11 February 2021). Product Disclosure Statement. Initial public offering of ordinary shares in My Food Bag Group Limited. My Food Bag's statements demonstrate that it looks to compete directly with supermarkets on price. That is consistent with our experience and why we disagree with the Draft Report's statements that meal-kits are not a competitive alternative for "more price sensitive" consumers (see [5.68]).

²⁴² My Food Bag's CEO says its "Kitchen" grocery delivery offering is expected to "tak[e] a greater share of New Zealand's substantial grocery spend." (20 August 2021). My Food Bag gets grilling from shareholders at first AGM since listing. The New Zealand Herald. Retrieved from:

<https://www.nzherald.co.nz/business/my-food-bag-gets-grilling-from-shareholders-at-first-agm-since-listing/SYC4FN6KOE3QMY3E3OSQQIXADA/>

strategy is to “tak[e] a greater share of New Zealanders’ substantial grocery spend” and “disrupt wider categories and channels”.²⁴³ See D18 below.

*Exhibit D18: My Food Bag’s stated growth strategy aspirations*²⁴⁴



30.2.4. HelloFresh,²⁴⁵ which in addition to its rapidly growing meal-kit service in New Zealand, is increasingly expanding overseas into offering “an accompanying online grocery store” called “HelloFresh Marketplace”, and (while its plans are developing) it “could envision such an offering growing to as many as 2,000 products over five years” with “a very, very clear path how you can get to 15% to 20% revenue share with those add-on products”,²⁴⁶ and

30.2.5. The Honest Grocer, Supie, and Four Candles Food Market.²⁴⁷

30.3. Beyond this range of grocery competitors operating differentiated business models, the reality is that two significant “bricks-and-mortar” competitors, Costco and The Warehouse, have entered to compete in the New Zealand retail grocery sector.

30.4. This recent entry demonstrates that it is only a matter of time before there is further entry and expansion, whether that be from Costco, The Warehouse, or international competitors (for example, Aldi) completing rollouts in other larger markets before expanding into New Zealand. To assist the Commission, we provide further information on these points as follows.

²⁴³ (20 August 2012). My Food Bag presentation to investors.

²⁴⁴ (20 August 2012). My Food Bag presentation to investors.

²⁴⁵ HelloFresh is increasingly expanding into online grocery delivery services in overseas markets through its “HelloFresh Marketplace” offering, which it is planning to continue to expand.

²⁴⁶ (4 May 2021). HelloFresh Moves to Expand Grocery Offering. Winsight Grocery Business. Retrieved from: <https://www.winsightgrocerybusiness.com/retailers/hellofresh-moves-expand-grocery-offering>

²⁴⁷ Four Candles Food Market is another new “bricks-and-mortar” grocery retailer that will be opening soon in Auckland - see: <https://fourcandles.co.nz/>

30.5. Costco will be a significant competitor:

- 30.5.1. The Draft Report says that the Commission does not consider that the entry of Costco will materially enhance competition - with Costco effectively treated as a fringe competitor. We disagree. We consider it inevitable that Costco will become a significant retail grocery competitor in New Zealand. The following points illustrate this.
- 30.5.2. Costco is the second largest “bricks-and-mortar” food / grocery retailer in the world with operations in 12 countries and sales of US\$163 billion in FY2020. It is a significantly larger retailer than Woolworths Group globally - it is more than five times larger than the Woolworths Group by market capitalisation.²⁴⁸
- 30.5.3. Costco stocks a comparable range of grocery products to that of major grocery retailers in New Zealand:
- 30.5.3.1. Costco’s offer includes: dry foods; packaged foods; groceries; snack foods; candy; alcoholic and non-alcoholic beverages; cleaning supplies; meat; produce; deli; bakery; health and beauty; apparel; garden; pharmacy (Countdown); petrol (FSNI / FSSI).
- 30.5.3.2. In FY20, food and beverage categories alone accounted for more than 56% of Costco’s sales (more than US\$91 billion).²⁴⁹ Therefore, core grocery is the majority of Costco’s business.
- 30.5.4. The nature of Costco’s proposition makes it highly relevant even to the Draft Report’s narrowly defined “main shop” definition:
- 30.5.4.1. Costco’s estimated average basket size ([] based on Australia analysis)²⁵⁰ is 2 to 3 times larger than the average Countdown basket, demonstrating that consumers use it as a “main shop”.
- 30.5.4.2. The introduction of an online delivery proposition, as Costco has done in other markets (Costco has an e-commerce offering in 8 of its markets), could easily expand Costco’s catchment in New Zealand beyond Auckland, Wellington and Christchurch where they are currently either building or intending to build stores.
- 30.5.4.3. Costco’s “pantry fill” proposition is, in some respects, the archetype of a “super-main shop”. When coupled with a rise in convenience shopping missions,²⁵¹ this is a good example of a way in which customer shopping behaviours are changing in a way that diminishes the relevance of a

²⁴⁸ AU\$49.17B (as at 30 July 2021) (<https://www2.asx.com.au/markets/company/wow>), compared to US\$189.97B (as at 30 July 2021) (<https://www.nasdaq.com/market-activity/stocks/cost>). AU\$ converted to US\$ at an exchange rate of AU\$1 = US0.73.

²⁴⁹ Costco FY2020 Annual Report. Available at: <https://investor.costco.com/static-files/7ef7bed6-c48f-4687-9c82-eb104b4823a5>.

²⁵⁰ [].

²⁵¹ As outlined in our Initial Submission, in New Zealand, the convenience trend is leading to significant changes in Kiwis’ shopping behaviour, such as the following

- shoppers are undertaking frequent, shorter in-store trips, versus large weekly shopping trips;
- there is increasing consumer demand for ready-made meals; and
- consumer expenditure on eating out and takeaway food is growing.

weekly “main shop”.

30.5.4.4. For Countdown, Costco is expected to resonate strongly with our target customer segments [] - amplifying their relevance as direct competition for any “main shop” trips.

30.5.5. Costco is successfully competing with grocery retailers globally and in Australia:

30.5.5.1. Costco has a loyal customer base with membership renewal rates at 91% in the US and Canada and 88% on a worldwide basis at the end of 2020.²⁵²

30.5.5.2. As of April 2020, Costco was the leading online grocery store in Japan,²⁵³ and the largest non-Korean owned retailer in Korea.²⁵⁴

30.5.5.3. Costco has an e-commerce offering in 8 of its markets which grew at 50% in FY2020.²⁵⁵

30.5.5.4. Costco entered Australia in 2009,²⁵⁶ and since then it has on average opened one new store per year (having recently opened its thirteenth store in Australia, and noting “there's lots more growth out there”).²⁵⁷ It is now ranked the second best *supermarket* brand in Australia in the 2020/21 Finder Retail Awards.²⁵⁸

30.5.6. As noted in the Draft Report,²⁵⁹ Costco is likely to seek a “price leadership” role in the New Zealand market:

30.5.6.1. For example, in Australia Costco is reported to be “25-30 per cent cheaper than other retailers”.²⁶⁰

30.5.6.2. The Commission's own consumer survey shows customers who have lived overseas use Costco as a benchmark for grocery price

²⁵² Costco FY2020 Annual Report. Available at:

<https://investor.costco.com/static-files/7ef7bed6-c48f-4687-9c82-eb104b4823a5>

²⁵³ Statista. Number of shoppers at major online grocery stores in Japan as of April 2020. Retrieved from:

<https://www.statista.com/statistics/1193127/japan-number-user-major-online-grocery-stores/>

²⁵⁴ Bank Meister website. Retrieved from:

<https://bankmeister.com/korea/shop/costco#:~:text=In%20Korea%2C%20Costco%20became%20the,for%20their%20%20membership%20before%20%20shopping>

²⁵⁵ Costco FY2020 Annual Report. Available at:

<https://investor.costco.com/static-files/7ef7bed6-c48f-4687-9c82-eb104b4823a5>

²⁵⁶ (26 February 2018) Costco to open its first Western Australia store. Australian Food News. Available at:

<https://www.ausfoodnews.com.au/2018/02/26/costco-to-open-its-first-western-australia-store.html>

²⁵⁷ (8 June 2021) Inside Costco's latest \$60 million 14,000 square metre warehouse opening in Lake Macquarie. 9 News. Available at:

<https://www.9news.com.au/national/costco-lake-macquarie-inside-new-warehouse-nsw-coast-newcastle/fbca90c1-3507-4d61-a1db-34cf9e7faed1>

²⁵⁸ (3 March 2021) The little-known chain that has upstaged rivals Aldi, Coles and Woolworths to be named the 'best supermarket in Australia' by thousands of shoppers. Daily Mail Australia. Available at:

<https://www.dailymail.co.uk/femail/article-9318505/Friendly-Grocer-upstages-rivals-ALDI-Coles-Woolworths-Costco-named-best-supermarket.html>

²⁵⁹ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [6.137].

²⁶⁰ (11 June 2019) Costco is coming to New Zealand, changing the way we shop. Stuff. Available at:

<https://www.stuff.co.nz/business/113355280/costco-is-coming-to-new-zealand>

comparisons.²⁶¹

30.5.7. The Draft Report's suggestion that Costco's "reasonably unique business model" diminishes either its relevance to assessing the likelihood of further new entry, or the competitive constraint it will place on other grocery retailers, is overly narrow. While Costco may operate a different floor-print and business model than Countdown, this business model is a key way in which Costco competes. For example, economic analysis in Australia has noted: "By bringing its unique retail model to Australia, Costco has substantially increased the level of competition in the retail market. The potential benefits for consumers relate to the likely price savings associated with this competition, and this encourages price reductions by other businesses as they adjust their operations to maintain market share."²⁶²

30.5.7.1. By the Draft Report's rationale, even a player like Aldi or Lidl could be marginalised for their relevance because they only offer a narrower range of largely private label SKUs.

30.5.7.2. Or if PAK'nSAVE were to hypothetically enter the market now, this rationale could be used to suggest that PAK'nSAVE's narrower range, low "cost-of-doing-business" fulfillment model, longer drive times, and larger basket sizes would somehow also mean that it was not a competitive constraint.

30.5.8. The Draft Report is incorrect in stating that Costco's "limited store network" in each of Auckland, Wellington, and Christchurch will mean that its competitive constraint is limited to "isolated catchment areas".²⁶³ Each Costco store has, on average, the floor space of 6 Countdown stores,²⁶⁴ so expansion by Costco to three stores would have the equivalent floor space of 18 Countdown stores. As the Draft Report notes, WWNZ has "seen analysis from Australia suggesting that Costco stores have in-person catchment areas of approximately 25 km."²⁶⁵ WWNZ estimates that with a store in each of those cities with a catchment of 25 km, Costco's catchment would cover ~40% of the New Zealand population. We would not characterise that as only covering "isolated catchments areas":

30.5.8.1. Even if we just take the 25km physical radius of its single Auckland store, this would amount to reaching approximately 1.1 million to 1.2 million Kiwis. See Exhibit D19 below.

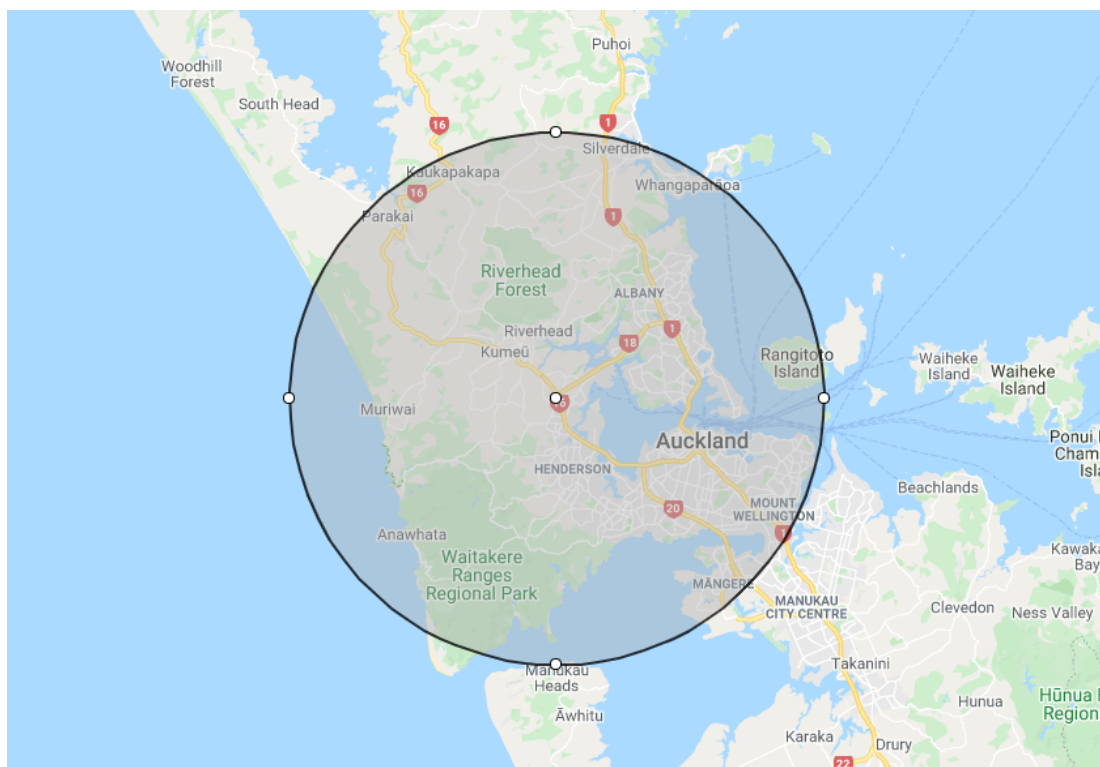
²⁶¹ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [F177].
²⁶² (10 November 2020). Costco Boolaroo. Economic Impact Assessment. Ethos Urban. On behalf of Costco Wholesale Australia Pty Ltd.

²⁶³ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [6.30.1] and [6.137.3].

²⁶⁴ WWNZ understands that, on average, a Costco store has floor space of 13,470 sqm.

²⁶⁵ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [4.105].

Exhibit D19: 25km radius around Costco's Auckland store



30.5.8.2. Furthermore, based on the population centres serviced by Costco stores internationally (for example, Costco has a store in Canberra - population 395,000), WWNZ estimates that Costco could establish more than five stores in New Zealand over time.

30.5.8.3. This is before one even considers the likelihood that in time Costco will introduce an e-commerce offering (as it has done in other markets - for example, in Australia it has launched online shopping and delivery, which would expand its coverage further if launched in New Zealand).²⁶⁶

30.5.9. We also note that other stakeholders view Costco as a core competitor to the major retailers. For example:

30.5.9.1. Respondents to the Commission's consumer survey consider Costco to be a major grocery retailer with many respondents who had previously lived overseas making comparisons on the price of groceries with "specific competitors such as Aldi or Costco."²⁶⁷

30.5.9.2. Katherine Rich, CEO of the New Zealand Food and Grocery Council, has stated (in a press release about the entry of Costco):²⁶⁸

²⁶⁶ (12 February 2020). Costco has announced it will launch members-only online shopping and delivery in Australia. Business Insider. Retrieved from: <https://www.businessinsider.com.au/costco-delivery-2020-2>

²⁶⁷ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [F17] - [F177].

²⁶⁸ New Zealand Food and Grocery Council. Retrieved from: <https://www.fgc.org.nz/costco-will-be-good-for-suppliers-consumers/>.

“This will be a win for suppliers and for consumers. Costco is another competitor for manufacturers to supply to, and they offer consumers another choice. “They offer a different retail format with their massive stores which have everything. Their bulk model works well in Australia and the US and I see no reason why it won’t work here. Buying in bulk is quite a different way of shopping but I think New Zealanders will welcome their heavily discounted offering.”

30.5.9.3. The United States Department of Agriculture has predicted that “the arrival of Costco to New Zealand, with their first store expected to open in Auckland in early 2022, will also increase competition in the sector as well as provide increased opportunities for U.S. food and beverages.”²⁶⁹

30.5.10. The actions WWNZ is mobilising in response to Costco’s entry demonstrates that Costco is considered to be a direct and significant competitor. For example, to help us compete with Costco’s imminent store opening in Westgate we have (amongst other things) [].

30.5.11. In terms of significant new entry to New Zealand, it is hard to imagine a new entrant more resourced and qualified to compete with WWNZ and Foodstuffs than the second largest “bricks-and-mortar” grocery retailer in the world.

30.6. The Warehouse is already a grocery retailer in New Zealand:

30.6.1. Despite what the Warehouse may have submitted to the Commission, it is also increasingly a competitor in the grocery retail space. It has a significant range of grocery products, and a significant nationwide store footprint (more than 90 “red shed” stores nationwide)²⁷⁰ and distribution network. The Warehouse’s CEO has stated it intends to become “the Amazon of New Zealand”.²⁷¹ The Warehouse actively (and increasingly) markets itself as having “more of NZ’s best grocery brands in store!” and having grocery aisles in its stores – see Exhibit D20 below.

²⁶⁹ (25 June 2021) Report from the USDA Foreign Agricultural Services. Retrieved from : [https://apps.fas.usda.gov/newgainapi/api/Report/DownloadReportByFileName?fileName=Retail%20Foods Wellington New%20Zealand_06-30-2021.pdf](https://apps.fas.usda.gov/newgainapi/api/Report/DownloadReportByFileName?fileName=Retail%20Foods%20Wellington%20New%20Zealand_06-30-2021.pdf).

²⁷⁰ The Warehouse. COVID-19 Updates. Retrieved from: <https://www.thewarehouse.co.nz/covid-19-updates>.

²⁷¹ (2 August 2019). New market realities and The Warehouse Group’s TheMarket. The Register. Retrieved from: <https://theregister.co.nz/2019/08/02/new-market-realities-and-warehouse-groups-themarket/>

Exhibit D20: Examples of The Warehouse promoting its grocery offering

Example of marketing
outside The Warehouse
Royal Oak on 8 May 2021



Example of marketing
inside The Warehouse
Royal Oak on 8 May 2021



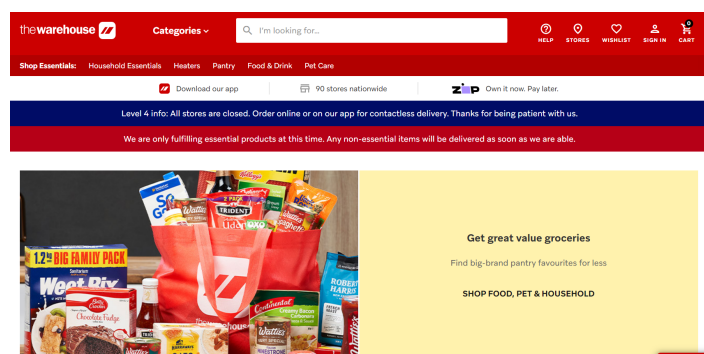
Image of a grocery aisle in
The Warehouse Lunn
Avenue on 18 July 2021



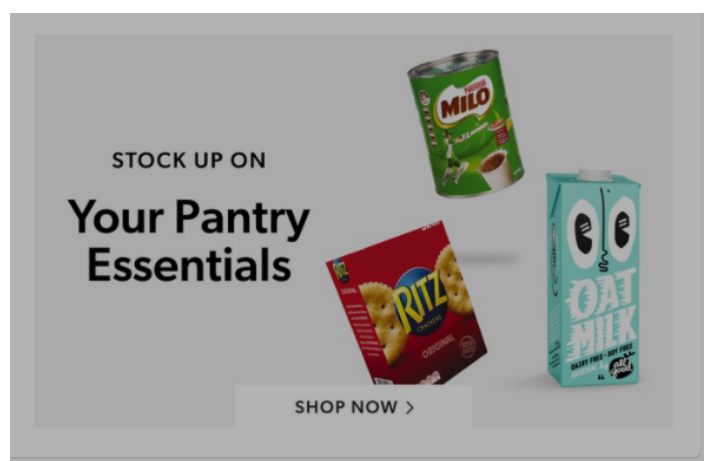
Image of a grocery aisle in The Warehouse Lunn Avenue on 18 July 2021



Screenshot of The Warehouse's homepage on 18 August 2021²⁷²



Screenshot of TheMarket's homepage on 18 August 2021²⁷³



²⁷² The Warehouse website. See: <https://www.thewarehouse.co.nz/>.

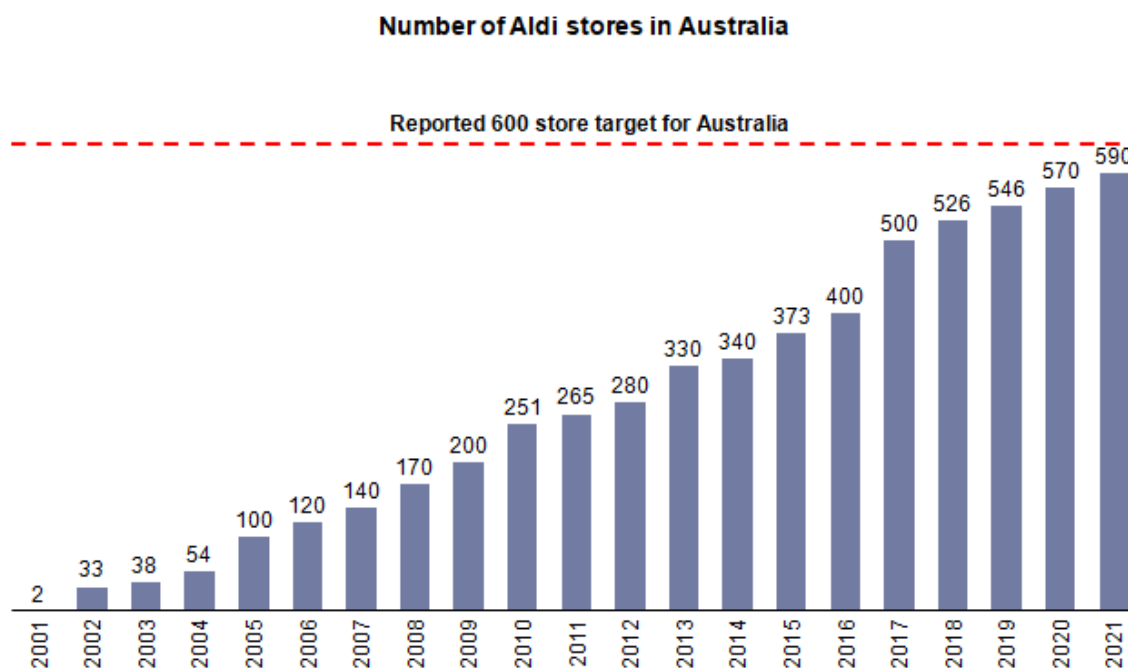
²⁷³ The Market website. See: <https://themarket.com/nz/>.

30.6.2. Moreover, The Warehouse has also announced plans to spend \$100 million to \$130 million per annum of capital expenditure over the next three years, including \$15 million to \$30 million per annum on its “supply chain” (including investments in its DC, a new central fulfilment centre, regional fulfilment centre, its warehouse management system, and order management system).²⁷⁴ The Warehouse is a significant business, with existing capabilities and expertise in managing retail supply chains - it could readily expand its retail grocery presence if it wanted to.²⁷⁵

30.7. In our view, it is inevitable that Aldi will enter New Zealand, and be a significant competitor:

30.7.1. While the Draft Report seems to have dismissed Aldi as a potential entrant in New Zealand, we certainly have not. The prospect of Aldi’s entry in New Zealand readily informs our strategic thinking. It has achieved significant and rapid expansion in Australia, including opening “24 stores in 2020 and plans to open 20 this year, taking its network to 590, just shy of the 600 stores the German based-discounter initially thought feasible.”²⁷⁶

*Exhibit D21: Number of Aldi stores in Australia*²⁷⁷



²⁷⁴ The Warehouse Group, Investor Day 2021 (4 May 2021). Retrieved from: https://www.thewarehousegroup.co.nz/application/files/4016/2016/4920/2021_Investor_Day_-_FINAL_WEBSITE.pdf

²⁷⁵ We also note that The Warehouse’s May 2021 Investor Presentation says that “building a customer ecosystem” is a strategic priority, and in outlining that strategic imperative The Warehouse management has advised investors that it looks at the “ecosystems” of retailers that have significant grocery businesses - including Walmart, Target, and Amazon. See: https://www.thewarehousegroup.co.nz/application/files/4016/2016/4920/2021_Investor_Day_-_FINAL_WEBSITE.pdf

²⁷⁶ (23 March 2021). Aldi eyes smaller stores, e-commerce as sales reach \$10.5b. Financial Review. Retrieved from: <https://www.afr.com/companies/retail/aldi-eyes-smaller-stores-e-commerce-as-sales-reach-10-5b-20210318-p57by3>

²⁷⁷ Various public sources.

- 30.7.2. Given Aldi's roll-out across Australia appears to now be complete, we expect expansion to New Zealand to be next on its horizon. Furthermore, while the Draft Report appears to rest on Aldi saying it does not have plans to enter New Zealand, we note Aldi similarly made statements in September 2009 and October 2012 denying plans to expand to Western Australia²⁷⁸ before announcing its expansion into Western Australia in February 2013.²⁷⁹ Aldi is known to have a policy of keeping its plans private.²⁸⁰ The fact that Aldi has made such a rapid expansion across Australia and is approaching its stated limit for Australia means its entry into New Zealand should be considered very likely, and as the Draft Report notes (consistent with competition case law) the "threat of entry by new firms" is itself a competitive constraint.²⁸¹ It is important that the Market Study take a forward looking and dynamic view of those competitors that are likely to increasingly impose competitive constraints in the near future (as it does in conducting merger analysis) in order to accurately assess competitive dynamics.
- 30.7.3. Moreover, as Aldi has established almost 600 stores in Australia, we do not consider the minimum benchmark for it to enter, identified in the Draft Report as 10 stores,²⁸² would be any impediment to its entry and expansion in New Zealand.
- 30.7.4. The rapid entry and expansion of Chemist Warehouse further demonstrates that Aldi would not likely encounter difficulties in establishing a footprint in New Zealand.²⁸³ Chemist Warehouse, which opened its first store in New Zealand in 2017²⁸⁴ and has an average store size of ~800 sqm (ranging between 600 sqm to over 1,000 sqm),²⁸⁵ is expected to reach 35 stores in New Zealand by the end of the year since (and has plans to expand to 70 stores nationwide).²⁸⁶ By comparison, the average size of an Aldi store in Australia is understood to be between about 900 sqm²⁸⁷ to 1,000 sqm.²⁸⁸

²⁷⁸ See for example:

- (19 September 2009). Reforms not enough to attract discount supermarket to WA. WA Today. Retrieved from: <https://www.watoday.com.au/national/western-australia/reforms-not-enough-to-attract-discount-supermarket-to-wa-20090918-fv7a.html>; and
- (25 October 2012). ALDI Continues to grow along the east coast. Australian Food News. Retrieved from: <https://www.ausfoodnews.com.au/2012/10/25/aldi-continues-to-grow-along-the-east-coast.html>

²⁷⁹ (12 February 2013). Western Australia and South Australia's cries for ALDI have been heard. Australian Food News. Retrieved from: <https://www.ausfoodnews.com.au/2013/02/12/western-australia-and-south-australia%E2%80%99s-cries-for-aldi-have-been-heard.html>

²⁸⁰ (9 October 2014). Aldi supermarket expansion in Australia prompts concern among independent retailers and butchers. ABC News. Retrieved from: <https://www.abc.net.au/news/rural/2014-10-09/nrn-aldi-expansion/5801608>

²⁸¹ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [6.2].

²⁸² Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [6.157].

²⁸³ The Draft Report did not include any reasons for its statement (at [6.39]) that The Chemist Warehouse would "likely face different sets of conditions of entry and expansion" to, say, Aldi.

²⁸⁴ (29 March 2021). Chemist Warehouse looks to regional areas for NZ growth. Inside Retail. Retrieved from: <https://insideretail.com.au/business/chemist-warehouse-looks-to-regional-areas-for-nz-growth-202103>

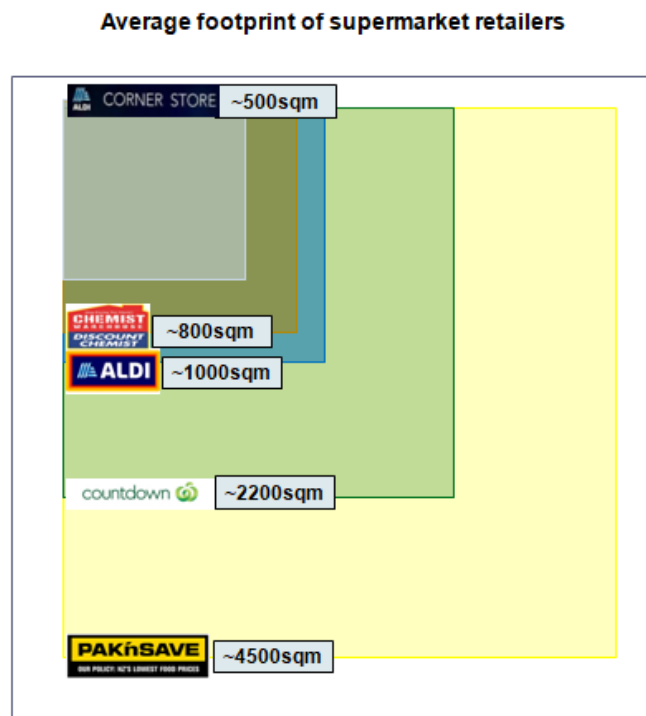
²⁸⁵ (9 April 2021). Chemist Warehouse to open branch at Christchurch's The Palms mall in spring. Stuff. Retrieved from: <https://www.stuff.co.nz/the-press/business/124754641/chemist-warehouse-to-open-branch-at-christchurchs-the-palms-mall-in-spring>

²⁸⁶ (5 March 2020). Australian pharmacy giant Chemist Warehouse to open in Christchurch. Stuff. Retrieved from: <https://www.stuff.co.nz/business/120003495/australian-pharmacy-giant-chemist-warehouse-to-open-in-christchurch>

²⁸⁷ (26 July 2008). Aldi's simple recipe for success. The Sydney Morning Herald. Retrieved from: <https://www.smh.com.au/business/aldis-simple-recipe-for-success-20080725-3l48.html>

²⁸⁸ (14 July 2021). Aldi launches new 'Corner Store' concept. Retail Analysis. <https://retailanalysis.igd.com/markets/australia/news/-news-article/t/aldi-launches-new-corner-store-concept/i/284>

Exhibit D22: Average footprint of supermarket retailers



- 30.7.5. The fact that Aldi's store footprint requirements are lower than larger supermarkets is well recognised in management literature as being one of its key competitive advantages:²⁸⁹

"Aldi's operational strategies and organisational routines are difficult to imitate as it focuses on its own generic brands, low store lease costs (Aldi only requires a small space, so it is flexible about where it can locate)....".

- 30.7.6. Moreover, Aldi has launched even smaller format stores in Australia,²⁹⁰ see Exhibit D23 below, with each such store "at around 500-600 sqm ... about half the size of a standard Aldi store."²⁹¹

⁵⁷ This article stated that Aldi's new "Aldi Corner Store" concept would "at around 500-600 sq m [be] about half the size of a standard Aldi store."

²⁸⁹ Strategic Management: thinking, analysis, action. By Graham Hubbard, John Rice, Peter Galvin. Melbourne, VIC : Pearson Australia, [2014] at page 111.

²⁹⁰ (23 March 2021). Aldi eyes smaller stores, e-commerce as sales reach \$10.5b. Financial Review. Retrieved from:

<https://www.afr.com/companies/retail/aldi-eyes-smaller-stores-e-commerce-as-sales-reach-10-5b-20210318-p57by3>

²⁹¹ (14 July 2021). Aldi launches new 'Corner Store' concept. Retail Analysis.

<https://retailanalysis.igd.com/markets/australia/news/-news-article/t/aldi-launches-new-corner-store-concept/i/28457>

Exhibit D23: Example of Aldi's small format "Aldi Corner Store" concept in Australia²⁹²



30.8. There have been a number of other new entrants, including Chemist Warehouse, The Honest Grocery, Supie, and meal-kit providers:

30.8.1. As noted in the Draft Report, there has been entry by a number of other competitors, including “meal kit providers and online-only grocery retailers such as The Honest Grocer and Supie”.²⁹³ The meal kit channel is estimated to be worth over [], and growing at more than [] per annum in New Zealand,²⁹⁴ with competitors offering a nationwide delivery presence (covering 86% of New Zealanders in the case of My Food Bag, and 84% in the case of HelloFresh).²⁹⁵

30.8.2. We also disagree with the Draft Report’s characterisation of Chemist Warehouse as a “single category retailer”.²⁹⁶ Chemist Warehouse operates across multiple categories including, health and beauty, baby, household cleaning and pharmaceutical needs, and its entry has had a clear impact on WWNZ’s sales. For example, in FY2020, health and beauty sales growth in our stores []. Given this, it is not correct for the Commission to suggest that we do not compete (or that there are barriers to entry or expansion for competitors such as this). In fact, particularly as trends away from the main-shop continue at pace, new entrants such as Chemist Warehouse or meal-kit providers pose a significant and accelerating part of our competitive dynamic.

²⁹² (19 July 2021). ALDI Corner Store by Landini Associates. Retail Design Blog. Retrieved from: <https://retaildesignblog.net/2021/07/19/aldi-corner-store-by-landini-associates/>.

²⁹³ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [3.153].

²⁹⁴ Indeed, HelloFresh is reported to have grown 159% in the last year. See: (4 February 2021). HelloFresh’s bumper year of New Zealand growth revealed. NZ Herald.

²⁹⁵ (4 February 2021). HelloFresh’s bumper year of New Zealand growth revealed. NZ Herald.

²⁹⁶ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [3.153].

30.9. In our view, the entry of Amazon in grocery retailing in New Zealand is almost inevitable:

- 30.9.1. In July 2021, Amazon announced that Amazon Australia would open to New Zealand customers. Amazon is the world's largest online retailer, acquired Wholefoods in 2017, and has been steadily building scale in both online and bricks-and-mortar grocery right across the globe (including its Amazon Fresh and Amazon Go grocery stores).
- 30.9.2. WWNZ considers it almost inevitable that Amazon will expand its grocery presence further in New Zealand, initially following the expansion path it has adopted in Australia where it is taking an increasingly prominent role in grocery retailing. In Australia, it is understood that Amazon:
- 30.9.2.1. already has a [] range overlap with Woolworths supermarkets (that is, [] of Woolworths' range is already available online via Amazon - either directly or via the Amazon marketplace);²⁹⁷
 - 30.9.2.2. had more than AU\$2.6bn of gross retail sales for the year to June 20, an increase of over 60%;²⁹⁸
 - 30.9.2.3. has an estimated [] monthly active app users and over [] Amazon Prime members in Australia;²⁹⁹ and
 - 30.9.2.4. will, over the course of 2020 and 2021, more than double its fulfilment capacity to 350,000 sqm in Australia.³⁰⁰

31. New entry to compete for the “main shop” is not reliant on an independent wholesaler

- 31.1. The Draft Report states that the lack of an “independent” wholesaler prevents other retailers from entering and expanding in competition with WWNZ and FSNI / FSSI supplied supermarkets. Observed market dynamics demonstrate that there does not need to be a separate “independent” wholesaler for entry / expansion to occur, and that new entry / expansion is inevitably likely from vertically integrated retailers that develop their own wholesaling functions. That is demonstrated by:
- 31.1.1. Costco's entry into the New Zealand grocery retail sector. That entry will occur without Costco relying on an existing wholesaler – it will form direct relationships with grocery suppliers in the same way WWNZ does.
 - 31.1.2. Aldi's entry and expansion in Australia, which has opened almost 590 stores across Australia since its arrival in Sydney in 2001 (opening on average 25 stores per year)

²⁹⁷ [].

²⁹⁸ (29 March 2021). Amazon Australia predicted to dominate local ecommerce by 2030. 9 News. Retrieved from:

<https://www.9news.com.au/national/amazon-australia-to-dominate-aussie-ecommerce-by-2030-analysts-predict/d68a5c85-2eaa-4686-9f8e-3c58a4eda9c6>

²⁹⁹ [].

³⁰⁰ (19 August 2020). Amazon expands Australian operations with fifth fulfilment centre. Australian Government. <https://www.austrade.gov.au/international/invest/investor-updates/2020/amazon-expands-australian-operations-with-fifth-fulfilment-centre>

without relying on an existing wholesaler.³⁰¹ Again, it has formed direct relationships with grocery suppliers in Australia rather than relying on a relationship with an independent wholesaler such as Metcash.

- 31.1.3. My Food Bag has rapidly expanded in New Zealand without relying on an existing wholesaler – rather it has “formed close relationships with our suppliers”.³⁰²
- 31.1.4. HelloFresh has similarly rapidly expanded in New Zealand without relying on an existing wholesaler – noting that it has “work[ed] closely with Kiwi farmers and suppliers wherever we can to source fresh, seasonal produce”.³⁰³
- 31.1.5. Farro Fresh has developed direct relationships “with over 550 local suppliers”,³⁰⁴ and is said to have plans to continue to expand.
- 31.1.6. The Warehouse is also understood to have formed direct relationships with a range of grocery suppliers to establish its “grocery aisles” across its network of The Warehouse stores (see Exhibit D20 above) by operating a “buying team” in a similar manner to WWNZ and other grocery retailers, with the majority of their grocery stock going through their DCs, and some products delivered direct to stores by suppliers (for example, bread and milk).
- 31.2. Given these examples, we do not agree with the suggestion in the Draft Report that new grocery retail entry or expansion in New Zealand would need to rely on an independent wholesaler.
- 31.3. We also do not agree that there are barriers to entry or expansion of a new grocery wholesaler. As the Draft Report notes “[t]here are also other independent foodservice wholesalers such as Bidfood and Service Foods”.³⁰⁵ The investment requirements (in terms of a distribution centre and access to logistics and transport providers) would be the same for a grocery and foodservice wholesaler, and both Bidfood and Service Foods have made such investments:
 - 31.3.1. “The Service Foods fleet, Distribution Centres and Processing Units are all temperature controlled and the cleanliness of our operations and vehicles are second to none”.³⁰⁶
 - 31.3.2. Bidfood has “over 2,200 staff operating from distribution centres and processing facilities in 17 regional locations from Whangarei to Invercargill”, including a 5,000 sqm temperature controlled distribution centre in Hamilton that opened in 2018 - see Exhibit D24 below.³⁰⁷

³⁰¹(21 March 2021) Aldi eyes smaller stores, e-commerce as sales reach \$10.5b. Financial Review. See: <https://www.afr.com/companies/retail/aldi-eyes-smaller-stores-e-commerce-as-sales-reach-10-5b-20210318-p57by3>

³⁰² My Food Bag. Product Disclosure Statement. 11 February 2021.

³⁰³ HelloFresh website. See: <https://www.hellofresh.co.nz/about/responsible-sourcing>

³⁰⁴ Farro Fresh - A Local Success Story. Ponsonby News. Available at: <http://www.ponsonbynews.co.nz/article-detail/show/598/>

³⁰⁵ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [2.52]

³⁰⁶ Service Foods’ website. Retrieved from: <https://www.servicefoods.co.nz/about>.

³⁰⁷ Archipro website. Retrieved from: <https://archipro.co.nz/project/bidfood-hamilton-temperature-controlled-distribution-centre-q-construction>.

*Exhibit D24: Image of Bidfood's temperature controlled distribution centre in Hamilton*³⁰⁸



- 31.4. Furthermore, Costco will become an additional wholesaler to other retailers - Costco is a significant wholesaler internationally and is predicted to be “a game changer not only in retail but also the wholesale sector” in New Zealand.³⁰⁹ Demonstrating this:
- 31.4.1. Economic analysis prepared on behalf of Costco has estimated that “sales to business customers are in the order of 30% of [its] total sales” in Australia and “include a high share of the following: Independent restaurants and take-away food outlets, Small supermarkets and convenience stores...”³¹⁰
- 31.4.2. In its 2017 consideration of the Tesco / Booker merger the UK Competition Markets Authority’s (**CMA**) decision referred to Costco among the key wholesalers in the UK, noting that “in cash and carry grocery wholesale, Booker and Bestway are the largest wholesalers in the UK, followed by Dhamecha, Blakemore, Parfett’s and Costco”.³¹¹
- 31.5. Accordingly, we do not agree with the views in the Draft Report that:
- 31.5.1. Costco could not be a potential wholesale supply option to independent grocery retailers due its pack-sizes or range (still estimated to be in excess of 3,700 SKUs).³¹²
- 31.5.2. Costco could not be considered a potential wholesale supply option due do its geographic location³¹³ - in particular, with respect to the cities where it is slated to enter (see paragraph 30.5 above), and particularly if it were to activate online

³⁰⁸ ArchiPro website. Retrieved from:

<https://archipro.co.nz/project/bidfood-hamilton-temperature-controlled-distribution-centre-q-construction>.

³⁰⁹ (4 January 2019). Warehouse retailer Costco still tipped to come to Auckland. Stuff. Retrieved from:

<https://www.stuff.co.nz/business/property/109729254/warehouse-chain-costco-still-tipped-to-come-to-auckland>

³¹⁰ (10 November 2020). Costco Boolaroo. Economic Impact Assessment. Ethos Urban. On behalf of Costco Wholesale Australia Pty Ltd.

³¹¹ UK CMA, “A report on the anticipated acquisition by Tesco PLC of Booker Group plc” (20 December 2017) at [7.66].

³¹² Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [6.137].

³¹³ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [6.137].

distribution. For example, Costco's Docklands store in Melbourne already offers delivery for business customers within 20 km, and further e-commerce enablement would rapidly achieve even greater wholesale reach.

- 31.5.3. Costco should be discounted as a potential wholesaler because the Commission "has not received any information regarding specific plans"³¹⁴ - the Commission's test should be to consider whether there would be any barriers to it becoming a wholesaler (which Costco's experience in Australia demonstrates there are none).

32. We do not consider that access to temperature controlled supply-chain logistics is a barrier to entry expansion

- 32.1. The Draft Report identifies that establishing logistics networks, such as temperature controlled distribution centres and supply chain arrangements, could be a barrier to entry in the New Zealand retail grocery sector.³¹⁵

- 32.2. We do not consider that this is the case. In particular, we, like other grocery retailers in New Zealand, largely rely on third party logistics providers for temperature controlled supply logistics. There is a large range of third party suppliers that specialise in providing both grocery suppliers and retailers with temperature controlled transport services by operating fleets of refrigerated vehicles and trailers, and chilled and frozen storage services (including cross-dock order picking, associated logistic, and consolidation services), by operating networks of cold storage facilities that use specialty warehouses equipped with large-scale freezers and / or cool rooms for the storage of temperature-sensitive products. For example (among many others):

- 32.2.1. Big Chill, which "operates a nationwide network of 9 modern, purpose-built depots covering 11,000 sqm", more than 200 chiller / freezer and trailer fleet.³¹⁶ Big Chill has stated that: "Big Chill's expansion into 3PL in Auckland will be a focus as well as taking advantage of a larger temperature-controlled Wellington hub. Customers will be able to benefit from a fully outsourced storage, picking & labelling service that links seamlessly into Big Chill's national delivery network."³¹⁷

- 32.2.2. Halls' Transport, which provides "an end-to-end service: integrating refrigerated and frozen transport, cold storage, cross-docking, warehousing and distribution"³¹⁸ and more than 500 specialist vehicles;³¹⁹

- 32.2.3. Refrigafreighters, which "ships chilled and frozen goods on our nationwide network. With our fleet of 140 trucks, trailers and combinations of dedicated refrigerated equipment we cover the North Island and South Islands with both metro and line haul services to the industry."³²⁰

- 32.2.4. Americold, "the world's largest publicly traded [Real Estate Investment Trust] focused on the ownership, operation, acquisition, and development of temperature-controlled

³¹⁴ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [6.136].

³¹⁵ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [6.142].

³¹⁶ (30 October 2019). Acquisition of Big Chill distribution. Retrieved from:

<http://nzx-prod-s7fsd7f98s.s3-website-ap-southeast-2.amazonaws.com/attachments/FRE/343468/310804.pdf>

³¹⁷ Freightways. Annual Report FY20. Retrieved from:

<https://www.freightways.co.nz/content/uploads/2020/09/FRE-Annual-Report-2020.pdf>

³¹⁸ Halls website. Retrieved from: <https://halls.co.nz/>

³¹⁹ Halls website. Retrieved from: <https://halls.co.nz/our-services>

³²⁰ Refrigafreighters website. Retrieved from: <http://www.refrigafreighters.co.nz/services.html>

warehouses”,³²¹ which is “adding capacity to support the expected growth of the national retailers, food producers, processors, distributors, and quick-service restaurants in New Zealand”.³²² Americold’s new expanded temperature-controlled warehousing facility in Auckland, that WWNZ has partnered with Americold to establish, has capacity to service both WWNZ as well as other third party customers - and Americold is currently advertising for customers to contract space in that facility. See Exhibit D25 below.

*Exhibit D25: Example of Americold advertising capacity in its expanded temperature-controlled warehousing facility in Auckland (25 August 2021)*³²³



32.2.5. Lineage Logistics New Zealand Ltd, which is a “wholly-owned subsidiary of United States-based Lineage Logistics LLC, the largest cold store supply chain company in

³²¹ Americold Press Release. Americold Realty Trust to Expand Infrastructure Network in New Zealand. (16 June 2020). Retrieved from: <https://ir.americold.com/news/news-details/2020/Americold-Realty-Trust-to-Expand-Infrastructure-Network-in-New-Zealand/default.aspx>

³²² Americold Press Release. Americold Realty Trust to Expand Infrastructure Network in New Zealand. (16 June 2020). Retrieved from: <https://ir.americold.com/news/news-details/2020/Americold-Realty-Trust-to-Expand-Infrastructure-Network-in-New-Zealand/default.aspx>

³²³ Personal details redacted.

the world”.³²⁴

- 32.3. We also note that during the COVID-19 lockdowns last year, The Warehouse was able to rapidly “set up a refrigerated last-mile delivery service” to support “TheMarket shift[ing] to selling fresh grocery food boxes.”³²⁵
- 32.4. Accordingly, we do not consider that access to logistics networks, such as temperature controlled distribution centres and supply chain arrangements, could be regarded as a barrier to entry in the New Zealand retail grocery sector.

33. The New Zealand grocery sector is innovative, with high-levels of online retailing, and significant investments in stores and supply chain

- 33.1. The preliminary finding in the Draft Report that New Zealand’s online grocery penetration, of 5.7%, is relatively low by international standards is incorrect.³²⁶ As is the preliminary finding that there has been limited innovation in the New Zealand retail sector³²⁷ (with the Draft Report suggesting that innovation in New Zealand “appears to be limited to the establishment of smaller store formats, the refurbishment of existing stores and developing new product offerings”).³²⁸
- 33.2. It is also difficult to reconcile the Draft Report’s statements that innovation is limited in New Zealand with its statements that the major grocery retailers in New Zealand are “focussed on product and service differentiation”³²⁹ and that “a significant emphasis is placed on growing market share through improving the quality of service, enhancing the overall shopping experience, managing stock levels, increasing product range and ensuring consistency in service levels across all stores.”³³⁰
- 33.3. The correct perspective is that, in many respects, WWNZ is an international leader in innovation, and New Zealand’s level of online grocery penetration is also close to world leading. At 5.7% in the Commission’s estimate, it is on par with Australia and Sweden, and exceeds the US, Germany, Italy and Spain.³³¹ Factoring population density (which, as noted in the Draft Report,³³² is an obvious and key determinant to feasibility and uptake of online retailing), our penetration is ahead of other similar countries.

³²⁴ (23 March 2021). Cool Investment Opportunity In Hawke’s Bay. Scoop. Retrieved from:

<https://www.scoop.co.nz/stories/BU2103/S00387/cool-investment-opportunity-in-hawkes-bay.htm>

³²⁵ (9 July 2020). TheMarket has doubled its range, reached over 165,000 in first year. Inside Retail. Retrieved from: <https://insideretail.co.nz/2020/07/09/themarket-has-doubled-its-range-reached-over-165000-in-first-year/>

³²⁶ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) figure 3.13.

³²⁷ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [3.5].

³²⁸ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [3.162].

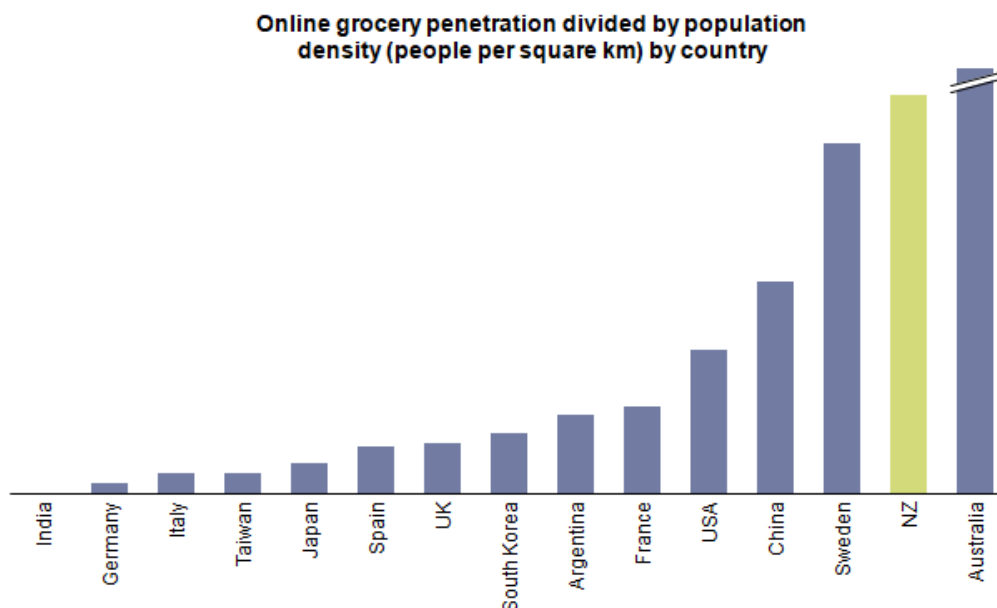
³²⁹ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [3.142].

³³⁰ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [4.58] and [5.45].

³³¹ Notably, while the Draft Report cited examples from the US and Australia to support a view that competition in those countries is fostering innovation, the US has lower online grocery penetration to New Zealand and Australia is almost identical.

³³² Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [6.43.4].

Exhibit D26: Online grocery penetration divided by population density (people per square km) by country³³³



33.4. Also:

- 33.4.1. The countries identified in the Draft Report as having greater online grocery penetration than New Zealand are also the countries that are known to have the highest rates of e-commerce penetration across all retail sectors (which suggests those rates are more likely reflective of societal trends, rather than any lack of innovation in the New Zealand retail grocery sector).
- 33.4.2. The Commission's use of 2020 as the comparison year for online grocery penetration in Figure 3.13 of the Draft Report fails to consider the distortion between countries caused by different COVID-19 dynamics. As the Commission will be aware New Zealand, compared to most other countries around the world (including the UK and France) had for most of the year no community transmission of COVID-19 in 2020 and, therefore, a comparatively very short period of COVID-19 lockdown and largely normal social movement for the rest of the year. Therefore, differences between the online penetration of New Zealand and, say, the UK in 2020 would likely be impacted by the UK's long-standing lockdowns during 2020. For example, while the Draft Report quotes the UK as having online grocery penetration of 11.4% in 2020, McKinsey has reported that this rate increased significantly from the previous year due to COVID-19: "UK grocery retailers for example saw their online share expand from 7.6 percent in 2019 to 11.2 percent in 2020 (reaching 13 percent market share at the highest point)."³³⁴ As has been observed in Europe: "We have seen that the more closed down society is [due to COVID-19], the more the online share goes up."³³⁵ Therefore, we do not consider that the Draft Report's comparison at Figure 3.13 is a fair or accurate "like-for-like" comparison given the different responses to, and impacts

³³³ Based on the online penetration rates cited in the Draft Report at Figure 3.13.

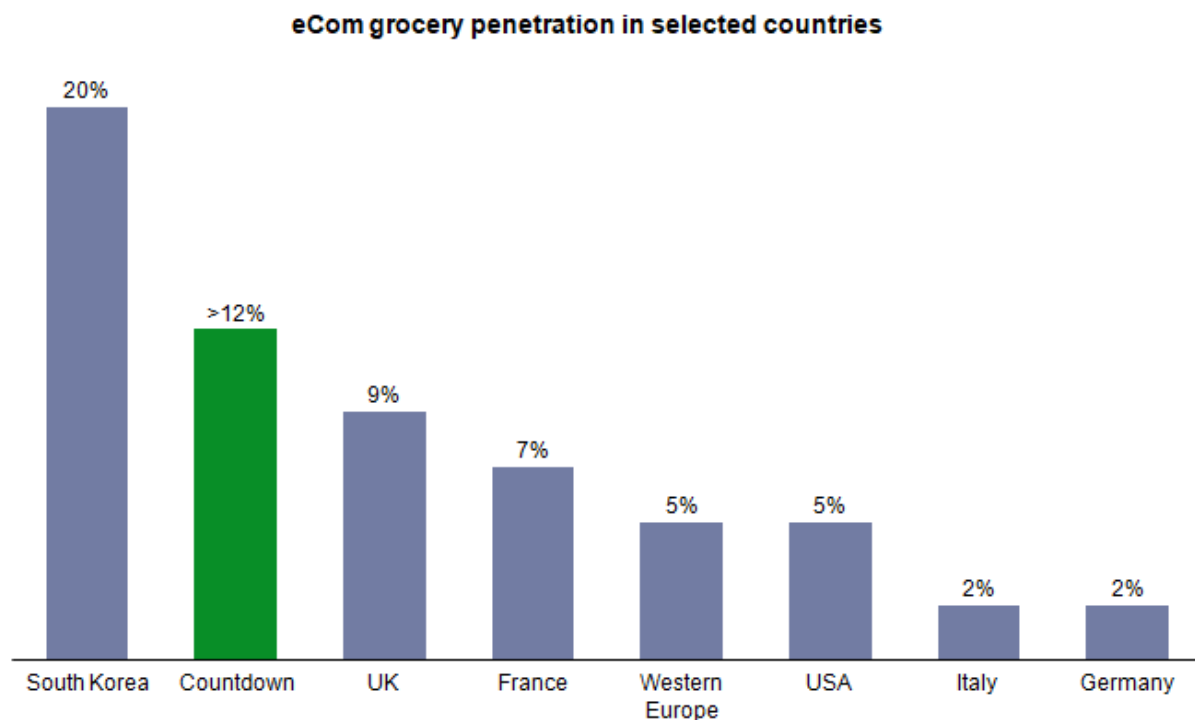
³³⁴ McKinsey. Disruption & Uncertainty. The State of Grocery Retail 2021. Europe.

³³⁵ Comment by Per Strömberg, CEO of ICA. McKinsey. Disruption & Uncertainty. The State of Grocery Retail 2021. Europe.

of, COVID-19 in 2020.

- 33.5. Even with those societal factors in New Zealand, Countdown (at more than 12% [])³³⁶ is one of the leading online grocery retailers internationally in line with or ahead of Tesco (12%) - and ahead of Kroger (8%), Walmart (11%), Costco (6%), and Ahold Delhaize (10%), and with penetration that exceeds that of many other countries (even when looking at 2020 data).³³⁷ See Exhibit D27 below.

Exhibit D27: eCom grocery penetration in selected countries compared to Countdown³³⁸



- 33.6. It also misses key dynamics to suggest that WWNZ (or the sector that it operates in) has not been innovative in online retailing by referring to FSNI and (in particular) FSSI's online model. WWNZ was one of the earliest adopters of online shopping in the world, with e-commerce orders first processed back in the late 1990s. While FSSI may be a later adopter of online grocery shopping, that is not a function of the level of competition or the sector or that "high profits are not acting as a reward for innovation in grocery retailing".³³⁹
- 33.7. Rather, it is almost inevitably a result of its cooperative / individual store owner model, which has meant its approach to online shopping needs to navigate different considerations to corporate grocery retailers - for example, determining local geographic territories for online delivery orders given each store is individually owned, coordinating digital platform investments across owner-operators, and navigating the tension between having two individual store owners operating under separate banners in the same local area. Illustrating that it is more difficult for a franchise / cooperative model to establish a broad online grocery offering, is the fact that:

³³⁶ Measured prior to the latest August 2021 Level 4 lockdown.

³³⁷ Deloitte, "Global Powers of Retailing 2021", at page 15.

³³⁸ Source: Bain: eCommerceDB. Note: 2020 data except South Korea which is 2019 data.

³³⁹ Commerce Commission "Market Study into the retail grocery sector – Draft Report" (29 July 2021) at [3.156].

- 33.7.1. in Australia the IGA banner only launched a nationwide online grocery service in May 2020;³⁴⁰ and
- 33.7.2. in the UK the Co-Op only began trialling an online offering in 2019 (which was limited to just London at that stage).³⁴¹
- 33.8. This dynamic has been noted by McKinsey (in its report McKinsey on Cooperatives) - that is, that "cooperatives are slower and less agile when it comes to renewing themselves (that is, their organisations change more slowly) than their publicly traded cousins."³⁴²
- 33.9. We have also already implemented, in effect, all of the examples of "international innovation" that the Draft Report incorrectly cited as missing from New Zealand and, therefore, evidence of "slower" or "modest" innovation in this country³⁴³ - see Exhibit D28 below. The fact that this is the case, despite the Draft Report seeking to cite a list of the most leading-edge innovations from around the world (and by some of the world's largest tech players such as Amazon and Alibaba), is testament to just how high the levels of innovation are in New Zealand (which is even more remarkable when the much smaller scale of the New Zealand market is taken into account).

Exhibit D28: WWNZ's responses to the Draft Report's examples of international innovations

Example of international innovation used in the Draft Report to suggest 'low' or 'modest' NZ innovation	WWNZ response
3.159 - the availability of drive through collection options (the Draft Report incorrectly states that "drive through" collection options are currently only available at Countdown Rototuna)	- Countdown already offers "drive" options across 19 stores. By the end of the calendar year this is expected to be [], with more than [] invested in drive-related rollouts this year alone. - A full "drive through" service is currently available in 4 stores: Rototuna, Te Rapa, Pokeno and Richmond, with 15 stores offering a dedicated 'drive up' solution. []. - Other related innovations already include extremely strong levels of same-day delivery and pick up, with [] of CD's online orders placed same-day, significantly higher than international benchmarks []. - Countdown is also investing extensively in automated pick-up locker solutions (and we note that non-automated pick up lockers are also widely in use across both New World and PAK'nSAVE). This includes a rollout of eLockers to [] stores by the end of this calendar year, and two automated Cleveron pick up units in place at Pukekohe South and Cambridge (among the first in the Southern Hemisphere, and in advance of the rest of the Woolworths Group). - We have also launched automated self-serve frozen, fresh and dry eLockers in the car parks of 18 stores.

³⁴⁰ (21 May 2020). IGA launches grocery delivery service. Franchise Business. Retrieved from: <https://www.franchisebusiness.com.au/iga-launches-grocery-delivery-service/>

³⁴¹ (22 March 2019). Co-op Group launches online food delivery service. Coop News. Retrieved from: <https://www.thenews.coop/137548/sector/retail/co-op-group-launches-online-food-delivery-service/>

³⁴² McKinsey & Company. McKinsey on Cooperatives (2012). Page 14.

³⁴³ It is also not accurate or robust for the Draft Report to cite "one off" innovations in overseas markets as evidence that, compared to those overseas markets, innovations in New Zealand "have not yet been adopted or implemented in any consistent or widespread manner across retail grocery stores". For example, we understand that the "living herb wall" and pick and mix bar dog treats is only in one small format Coles Local store in St Kilda, so is not an example of "consistent or widespread" innovation compared to New Zealand. We also note that the "living herb wall" was understood to be a failure, and was withdrawn from that store.

3.161.1 - investments in the use of personal shoppers and building small store formats in response to consumer demand for convenience and personalised shopping experiences	• WWNZ has already opened two Metro small format stores in the last two years, and is scheduled to open further small format innovations in Herne Bay (neighborhood metro) and Wanaka (a New Zealand first metro / pick-up hybrid) this year. • The use of personal shoppers underpins Countdown's world-leading online penetration rates (see paragraphs 33.3 to 33.5 above). We employ over 2,000 personal shoppers across our stores and now eStores (with 73% of shoppers scoring our online service a 9 or 10 out of 10).
3.161.2 - the development of in-store shopping experiences [by Hema] such as the use of barcodes on price tickets that allow consumers to scan the product barcode instantly and see the price and review of the item online using the store's mobile app	• Hema in China is the tech-enabled grocery retail pilot of Alibaba, one of the largest tech companies and retailers in the world. Despite Alibaba being many times bigger than we are, we are proud to have delivered a number of comparable innovations. Namely: ○ Over [] customers use Countdown's App every week - an increase of over [] in just the last year. This App allows customers to scan their digital Onecard, transact in-App, locate products by individual aisle by store, create and share shopping lists (also organised by aisle), access personalised Boosts, check prices, access e-receipts, and more. ○ Countdown has also launched The Bunch - an online review community with over 10,000 members. These members have already provided over [] reviews on over [] products - with selected product reviews also highlighted in store. ○ Countdown worked with Affinity ID to develop and launch a world-first personalised online mailer.³⁴⁴ • Countdown has not implemented Hema's facial recognition checkout technology due to different privacy practices and consumer expectations. However, we have introduced AI-driven product camera technology into our self-checkouts at 22 stores to make it faster for customers to select drop down-menus during the self-checkout experience. We also note that electronic shelf labels (ESLs) are already prevalent in the New Zealand grocery market, with Countdown currently testing next-generation ESLs for rollout to [] stores by end of this financial year.
3.161.3 - new cashierless stores in the US and UK (Amazon Go Grocery) that uses high-tech sensors to identify what consumers pick up from the aisles, creating a checkout-free shopping option for consumers 3.160 - technological advances such as mobile checkouts and the use of apps to enable consumers to connect to personal shoppers	• We note that Amazon is the world's largest retailer and one of the largest tech companies in the world. Despite Amazon being many times bigger than we are, we have delivered a number of comparable innovations: ○ Countdown has launched a contactless "Scan & Go" service with this already in 6 stores and expected to be rolled out to [] by the end of this financial year. This solution uses high-tech scales, sensor technology and to detect what our customers are buying and enable a check-out free shopping experience. ○ We have also implemented self-scan checkout technology with over 1,150 self-checkout kiosks available across the Countdown store network and over 80 self-checkout kiosks in the SuperValue FreshChoice network. Our self-checkout innovation includes the planned rollout of new image-based technology to make drop-down selection of fresh products even easier for our customers. • We also note that other players in the New Zealand grocery market have also delivered innovative checkout solutions, with Shop n Go technology available across a number of New World and PAK'nSAVE stores, and for some time. • In addition to the mobile app innovations outlined earlier in this table, we also note that customers are able to engage directly with Olive, Countdown's AI-driven chatbot via the mobile app, for answers to their most frequent queries, and for automated refunds.
3.161.4 - the development of innovative store features to tailor	• Our development of innovative in-store features is extensive, and frequently informed by local catchment attributes. This includes but is not

³⁴⁴ Digitas Affinity ID website. Retrieved from: <https://www.digitasaffinity.id/case-studies/mycountdown/>

the retail offer to local demographics, such as Coles adding store-specific innovative features such as a living herb wall, a pick and mix bar for dog treats, and stocking a large range of vegan and vegetarian products	limited to: ○ dedicated health foods sections in over 170 stores; ○ produce misting in 38 stores; ○ new promotional ends rolled out to ~170 stores to improve shopability and productivity; ○ new deli equipment rolled out to 149 stores over the past two years to improve display and reduce stock loss; ○ 37 instore pharmacies; and ○ new value-oriented pallet displays in 4 stores to date. ● We are also constantly testing-and-learning through innovative instore pilots. Examples include our “Unpacked” plastic-free-produce pilot; kitchenware and apparel category pilots; healthy checkout pilots; healthy-living display ends; Onecard kiosks; flatbread ovens; flame-roasted chickens; ready-to-eat foods and more. ● Other in-store innovations we have observed across the grocery market (even just focussing on the Commission's major grocery retailers) include but are not limited to: wholefoods bulk-bins; salad bars; aged meat displays; wine cellars; piano bars; in-store sushi; and regional product displays. ● We would also like to note, Coles’ “living herb wall” proved unsuccessful and was removed. Woolworths Australia also tried a similar concept that was equally unsuccessful. Hence WWNZ’s decision not to instal “living herb walls” in our stores.
3.161.5 - widespread use of grocery robots at supermarket chains such as Giant and Stop & Shop in the US that alerts consumers to potential hazards such as spills and monitor shelves to alert workers to out-of-stock items and other problems relating to merchandise presentation.	● As discussed in our preliminary issues paper, Countdown’s Rototuna store already includes exactly this example of an in-store grocery robot to notify the team of any spills and hazards and identify gaps in the shelves to improve availability. ● Countdown’s Rototuna store also includes a dispensing robot for greater speed and accuracy in our in-store pharmacy, as well as advanced and innovative temperature monitoring solutions to track and optimise refrigeration and product quality.

33.10. We are committed to innovation, and we have invested in a number of other innovations (including world-leading innovations) in our Countdown business. Reflecting this, in 2018 we established a new division within our business called CountdownX. This technology / innovation division has 250 staff and manages the digital aspects of our retail business, including online shopping, the Onecard loyalty programme, digital marketing and customer care.³⁴⁵ This significant digital capability was particularly essential to ensuring continuity of supply to New Zealand customers during the COVID-19 lockdowns of 2020 as we were forced to make major business decisions at speed, and rapidly add scale to our online grocery capacity. For example, the CountdownX team’s work on its online platforms enabled:

33.10.1. A 60% expansion in online shopping capacity for Countdown within a matter of weeks during the first COVID-19 lockdown of 2020.

33.10.2. The processing of 120,000 applications for priority access via Countdown’s website.

33.10.3. The launch of a pilot e-queue system in April 2020, that would allow people to wait in their cars rather than line up in the carpark for their turn to enter a Countdown store. We developed that proposition in-house in less than a week.

33.10.4. The mass online launch for SuperValue / FreshChoice stores in response to COVID-19 and WWNZ seeing the need to use digital channels to serve Kiwis - that

³⁴⁵ We also recently launched the Compass app, which is free for our suppliers, to provide them with real-time data about their products to assist them to make decisions about their supply chain.

project enabled an online proposition to be launched for 40 stores within a two month window (with that project implemented by a 40+ person project team that was stood-up in less than 24 hours).

33.11. What we were able to do during that short period of time is, from our perspective, testament to our dedication to innovation. Our whole technology, website and fulfilment systems had to be rapidly scaled to enable us to cope.

33.12. This commitment to innovation was recognised at the 2020 New Zealand CIO awards.³⁴⁶ Sally Copland (our General Manager of Brand and CountdownX) was named New Zealand CIO of the Year, and CountdownX was recognised as a finalist in the Business Transformation through Digital and IT category for its initial COVID-19 response.³⁴⁷

33.13. We are also continuing to invest significantly into our digital capability. This includes establishing four eStores, including dedicated sites purpose-built to support world-leading micro-fulfilment capabilities to enhance efficiency and resilience of the “last mile” of our online grocery supply chain (that is, from the warehouse or store to our customers).

33.14. It is not just in the digital space that we continue to invest and innovate - it is also in our supply chain and store network:

33.14.1. We invest to provide New Zealand an efficient and resilient supply chain: We have made, and continue to make, significant investments in our integrated supply chain and logistics capabilities. We make these investments to ensure our network can meet supply chain requirements and efficiently meet our customers’ needs. Consumers benefit significantly from these investments. The enhanced efficiencies we have achieved have helped us to reduce our retail prices (in real terms) over the last decade, deliver improved service and quality outcomes, and provide us with the capability and resilience to deal with unexpected shocks to either supply or demand. They also help mitigate supply chain cost increases that would otherwise occur (estimated at [] over the next 6 to 7 years). There are a number of significant logistics projects currently underway or approaching completion with an estimated capital investment of approximately [] (from both WWNZ and our partners). This includes:

33.14.1.1. Developing a new purpose-built 38,000 sqm distribution centre in Palmerston North to service the lower North Island. This \$100 million project has opened from August 2021, and will deliver 70 new jobs, a number of energy and water efficiency initiatives (for example, rainwater harvesting), and significantly improved on-shelf-availability, service levels, and supply chain resilience for the Lower North Island by holding 7,000 SKUs (compared to 1,700 SKUs previously).

33.14.1.2. Partnering with Hilton Food Group, to establish a brand new, state of the -art, \$100 million meat processing plant in Auckland, with “go-live” commencing in July 2021.³⁴⁸ This includes innovative new products

³⁴⁶ The New Zealand CIO Awards celebrate innovation and success in the ICT industry.

³⁴⁷ Countdown News and Media Releases (25 November 2020) Countdown’s COVID approach awarded at NZ CIO Awards. Available at: <https://www.countdown.co.nz/news-and-media-releases/2020/november/countdown-s-covid-approach-awarded-a-t-nz-cio-awards>

³⁴⁸ (11 April 2019). A \$100m hi-tech meat processing facility is to be built at Wiri to supply Countdown North Island. Stuff. Retrieved from:

(including ready meal SKUs), new packaging (for example, sealed fresh packaging that improves shelf-life and product quality), and new distribution (for example, new crates, robotic sorting, and co-distribution with fresh produce to drive efficiencies).

33.14.1.3. Partnering with Americold to establish a \$65 million expanded temperature-controlled warehousing facility in Auckland (“go-live” July 2021).

33.14.1.4. Developing a new state-of-the-art 20,000 sqm produce distribution centre in Auckland (“go-live” in FY2022) to help service all of Countdown’s North Island stores with fresh fruit and vegetables direct from local growers ([]). This includes improved cold chain management to deliver better quality outcomes for customers.

33.14.1.5. [].

33.14.2. We invest in our stores to provide attractive, and sustainable, shopping environments: We invest over [] per annum in building new stores, upgrading our existing stores and launching new formats (we also partner with our landlords, through our leases, to enable further significant investment from landlords in store development that is not included in this figure). We have a large pipeline of store renewals planned [] and, as noted in Exhibit D28 above, we have launched our small-format Metro stores to meet customers’ demand for convenience. Our investments in store renewals and innovation is consistent with the Commission’s observation in the Draft Report that the evidence is “that the major grocery retailers do extensive research to understand how their retail grocery offer matches consumers’ needs so that they can maximise store attractiveness and fulfil every different type of shopping mission”.³⁴⁹ That is evidence that we care, and care deeply, about innovating our offering to best meet our customers’ expectations. We have also announced ambitious new sustainability goals that we have set to achieve by 2025 (*Kia pai ake te āpōpō - A Better Tomorrow*), including making a commitment on zero food waste to landfill from our stores by 2025; developing and building our supermarkets and distribution centres in more sustainable ways including a 5 Green Star rating for all new stores from 2025; and cutting carbon emissions dramatically (we have already reduced our emissions by more than 25% since 2016 through things like energy efficient refrigeration systems, LED lighting, and reducing food waste to landfill). For these reasons, our new stores include a number of innovative sustainability features. For example our new Richmond Countdown store (that opened in June 2021) includes the following emissions, water, paper and energy saving features:³⁵⁰

33.14.2.1. solar panels that will generate 10% to 15% of the store’s total energy;

33.14.2.2. transcritical refrigeration systems that use natural refrigerant gases;

<https://www.stuff.co.nz/business/111899901/a-100m-hitech-meat-processing-facility-is-to-be-built-at-wiri-to-supply-countdown-north-island>

³⁴⁹ Commerce Commission “Market Study into the retail grocery sector – Draft Report” (29 July 2021) at [4.74].

³⁵⁰ Countdown News and Media Releases (25 June 2021) Countdown opens its greenest store with solar panels, planet-friendly fridges and EV parks galore. Available at: <https://www.countdown.co.nz/news-and-media-releases/2021/june/countdown-opens-its-greenest-store-with-solar-panels-planet-friendly-fridges-and-ev-parks-galore>

- 33.14.2.3. LED lighting which is 35% more efficient than traditional lighting;
 - 33.14.2.4. water-saving taps to reduce water use;
 - 33.14.2.5. an Energy Management System, which provides regular updates on store energy and water use;
 - 33.14.2.6. doors on fridges and freezers to reduce energy use - every 10 doors saves enough energy to power a NZ home for a year;
 - 33.14.2.7. digital shelf labels to reduce paper use;
 - 33.14.2.8. EV chargers for customer cars;
 - 33.14.2.9. electric online delivery truck; and
 - 33.14.2.10. plenty of bike parks to help reduce short car trips to the store.
- 33.15. To assist the Commission to better understand the innovations in our business, and the investment we have made to improve our customers' experiences shopping with us and the efficiency of our supply, we invite the Commission to visit some of our sites. For example, we invite the Commission to visit our Countdown Richmond store or our Countdown Rotorua store, or to have a tour of one of our online "dark stores" or one of our distribution centres.