

## SUBMISSION

### BY METCASH TO THE LEGISLATIVE ASSEMBLY FOR THE ACT

#### SELECT COMMITTEE ON ACT SUPERMARKET COMPETITION POLICY

This submission is prepared in response to the transcript of evidence given by James Koundouris from the Supabarn Group and Chris Haridemos the owner of the Supermarket at Kaleen to the above committee on the 19<sup>th</sup> of April 2012.

#### **WHOLESALE MARKET IN THE ACT**

Mr Koundouris gave evidence asserting that Metcash has a monopoly in the wholesale of groceries in Australia and that we Metcash terminated supply to the Supabarn Group in November 2011. These statements are false.

Metcash understands Supabarn to be part supplied by SPAR a competitor to Metcash and notes from the evidence of Mr Koundouris that the Supabarn Group is in the process of establishing its own wholesale business.

An ACT based wholesale business is not financially viable because of the lack of scale available in the ACT. It is a matter of public record that Franklins, with 90 supermarkets in and around Sydney, was not viable.

#### **FLOORSPACE DOMINANCE TEST**

The ACT Governments over time have undertaken a series of reviews of supermarket policy, all of which have been focussed on maintaining a competitive supermarket sector for the residents of the ACT. The ACT has the greatest level of domination in the supermarket sector of any capital city in Australia. Woolworths has 50% of the total market in the ACT, which is nationally the highest share for any capital city.

Metcash and the IGA retailer network made a written submission to the Martin Review which recommended that a Floorspace Dominance Test (FDT) be adopted by the ACT planning system. Enclosed is a copy of that submission.

A FDT would ensure that the ACT planning system had the tools to ensure that competition was encouraged in the supermarket sector.

The FDT was rejected by the Martin Report.

Subsequent to the Martin Report, the major chains expansion plans in the ACT continued. Woolworths opened a 800sqm store in Dunlop and we understand has purchased the supermarket site at Bonner. Woolworths has also sort to build new supermarkets at Lawson and Giralang. It seems clear from these actions that Woolworths is seeking to dominant the ACT market north of the lake as it already does south of the lake.

The Chief Minister Stanhope announced that the ACT Government would give serious consideration to implementing a FDT shortly before resigning.

Any suggestion to this Committee that Metcash sought an increase in local centres from 1,000 sqm to 1,500sqm is false. At all times Metcash has supported and continues to support the adoption of the FDT. It is the most effective way to encourage competition in the supermarket sector and is consistent with the planning principles of the ACT.

Metcash pointed out to Mr Martin during his review that increasing the size of local centre supermarkets invited the major chains into those centre. And this is what has happened at Dunlop.

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# **Enhancing retail competition through the planning system**

## ***Discussion paper***

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## **Background**

The Australian retail sector is subject to very high levels of concentration, particularly in the food and grocery industry, predominantly associated with Coles and Woolworths. In addition to these high levels of concentration, which by some measures reach at least 70% (ACCC findings into the competitiveness of retail prices the standard groceries, 2008) there are regions where virtual market dominance has been achieved by one or other of these major players.

Although some jurisdictions are looking to minimise the role of planning when it comes to managing the retail sector, this approach has substantial risks. For example, in NSW, it is proposed to create a virtual "open market" in terms of the supply of zoned commercial land. On the evidence, however, this would serve to further reinforce the incumbents rather than create significant opportunities for new entrants. In part this relates to land banking of sites that has already occurred, and also the ability of the incumbents to move quickly when opportunities arise as a result of their financial capacity and existing infrastructure.

The natural tendency of the capitalist firm is towards monopoly. It is therefore necessary to maintain competitive conditions through intervention of government. In this respect there is the role played by Federal legislation, particularly the Trade Practices Act, however as presently drafted this Act has a limited ability to manage market concentration, particularly on a regional and sub-regional level. This leaves the planning system as the only available and effective tool. This is acknowledged in the ACCC Grocery Review (see page 241).

## **Role of the planning system**

A key issue is whether justification exists for the use of the planning system in this way. Irrespective of jurisdiction, the notion of "net community benefit" underpins the notion of planning, and provides, in the context of national competition policy, justification for intervention by way of regulation in the operation of the land use system/market. Clearly, within the framework of national competition policy, the furthering of competition is an important community benefit, provided this competition is not to the overall detriment of planning objectives that seek social, environmental and welfare outcomes for communities. In other words, the overall outcome for the community needs to be positive, recognising that achieving some positive outcomes may result in these being partially offset by other negative outcomes.

The key planning mechanisms to assist improve competition are the creation of a level playing field so that both incumbents and new entrants face the same regulatory environment (predominantly through land-use zoning and tools such as parking policies) and, further, to avoid the situation where single players are able to gain excessive dominance within a sub-market.

There is clear evidence that where "regionalisation" occurs in terms of market dominance grocery prices are higher. The ACCC in its enquiry into the competitiveness of retail prices (2008) identified patterns of relationship between nearby competition and prices (see pages 61 – 68 and 115, 116, 174, 175, 206, 208). Work carried out by Dr. Robert Baker at the University of New England suggests that the differential could be in the order of some 6%. (The Hilmer paradox: Evidence from the Australian retail grocery industry, 1998).

On this basis we have a prime face justification for the use of planning tools to address market dominance.

## **Tools to address market dominance**

### ***Measuring market dominance***

Planning tools, by their nature, will always be somewhat imprecise in their ability to achieve their intended outcomes. In many cases, "pure" planning principles are difficult to apply, in particular in terms of available information. This is very much the case with the retail sector where one of the key pieces of information, turnover per square metre per retail outlet is "commercial in confidence" information.

Even if this information were available, verification would be very difficult. Accordingly, the preferable measurement tool in terms of assessing issues such as market dominance becomes floorspace. Floorspace can be measured in a variety of ways, including net selling space and, more commonly, gross leasable floor space. Whilst net selling space is probably a better overall measure, gross leasable floor space is a reasonable surrogate that is easily and cheaply available.

The floorspace measurement tool can be used as an aggregate tool to address overall dominance in the total market, noting that the ACCC enquiry into the competitiveness of retail prices (2008) identified concentrations within different sub-sectors of the food and grocery market ranging from 20%-70%.

Floorspace tools could be utilised to assess sub-markets such as packaged groceries, fresh fruit and vegetables and the like. In practice, however, a straightforward measure of the percentage of overall gross leasable floor space owned or controlled by a single retail operator within a catchment provides an easily discernible figure that is difficult to challenge. Categorisation of the different floorspaces for different sub uses is more difficult, and prone to differences in interpretation. For example, there are wide variations in floorspace intensity of use when examining packaged groceries as compared to fruit and vegetables where shelf space per square metre is considerably higher for packaged groceries.

With respect to the determination of catchments, some issues arise. These include the spatial scale of catchments appropriate for study and also determining the boundaries of those catchments. There are a range of criteria for determining primary trade areas for retail centres of different size which are routinely applied as part of economic evaluations of new retail developments. Whilst there is a degree of professional judgement involved in these determinations, results tend to be reasonably consistent.

It is suggested that catchment determination would be best undertaken by government, based on a set of criteria generally agreed by the retail industry. These would be based on the commonly accepted tools and could, it is suggested, operate usefully at the regional level. In this regard, catchments for determining market domination could be based on the primary trade area of the highest order regional activity centres with adjustments made to recognise overlapping.

The key factors for determining trade areas include:

- Floorspace,
- Range,
- Facilities,
- Brand loyalty,
- Intervening opportunity,

- Destination versus incidental shopping,
- Socioeconomic status, and
- Physical and psychological barriers to movement.

### ***Enhancing competition***

For competition to operate effectively, there needs to be consideration given to competition within centres, as well as competition between centres.

### **Competition within centres**

#### **Neighbourhood centres**

In the case of neighbourhood centres, for example, an uncompetitive environment arises where a neighbourhood centre consists of a single supermarket and "tied" specialties, e.g. liquor. A balanced neighbourhood centre would generally have some 30-50% of its floorspace as supermarket, providing scope for specialty stores to co-locate to assist to both improve the range of offer and improve competition. Synergistic benefits occur where a larger retail anchor provides the "drawing power" to assist specialty shopping. In this respect a supermarket anchor in the order of 850-1250 m<sup>2</sup> is adequate to provide drawing power, whilst still allowing overall floor space of a neighbourhood centre to sit below the 1700-2500 m<sup>2</sup> threshold which defines a good walkable centre. Overall consumer benefits are maximised when this occurs, as the need for car travel is minimised whilst still providing a competitive retail environment for most daily needs.

#### **District centres**

For larger centres, such as district centres, it is usual to expect two to three supermarkets, which, ideally, should have different operators although at the present time there is nothing to constrain multiple supermarkets in the same retail "stable" operating in a single district centre (for example a Coles and a Bi-Lo).

### **Competition between centres**

Competition between centres means ensuring that market dominance does not occur, in terms of the main retail anchors in competing centres, and in terms of the ownership of those centres. This also relates to the identification of appropriate sub-markets and looking at the market dominance of single retail operators within that area. For example, taking the Belconnen region in the ACT, we have a situation of a dominant regional centre supported by a network of neighbourhood centres of varying levels of performance. Ideally a range of operators should be anchoring the neighbourhood centres, whilst at the regional centre level a mixture of operators should occur in the centre, as should also occur in other competing regional centres.

A further issue here with respect to competing regional centres is the issue of the centre ownership. At the present time there is no control that would prevent a single centre owner developing and operating the majority of centres within an overall city or metropolitan catchment such as the ACT. This, potentially, is a significant anti-competitive issue where the gross leasable floorspace tool could also be utilised on a broader spatial scale.

### ***Use of the floorspace measure***

The floorspace measure can be utilised to determine market dominance at all spatial scales, as necessary. In practice, it would be expected that the focus would be on the regional/subregional level. For example, taking the ACT as a whole would be insufficiently detailed to provide a full

understanding of dominance at the regional and sub-regional (district) level, although an overall "picture" of the whole ACT could be obtained, including the degree of single ownership of regional centres. For this reason, regional catchments should be the main focus of analysis, as they can easily be aggregated up to cover the whole jurisdiction.

Further reinforcement for consideration at this spatial scale comes from the theory of indifference curves. In practice, once people are in their car, they are relatively indifferent to travel times up to approximately 15 minutes. This would allow access to several neighbourhood centres within a reasonable radius, and represents common driving times between regional centres.

### ***The floorspace dominance test***

The suggested measure to facilitate competition is the use of a "floorspace dominance test" relating to each retail operator within its market. In this respect, although supermarket concentration is often raised as the primary anti-competitive issue, the use of a floorspace dominance test should operate across all portions of the retail sector. It is noted that care is needed from a definitional point of view, as retailing follows traditional categories to a lesser and lesser extent. In particular, for what might be termed commodity purchases (known, predictable, routine) there is a strong move towards stores spanning multiple categories of goods. For example the supermarket now sells clothing, electrical goods, hardware items and the like and we are also seeing the emergence of USA style hypermarkets which blur the boundaries between a discount department store and supermarket.

By looking at the totality of floorspace owned or managed by a particular retail operator, and then desegregating into main retail categories (utilizing ANZSIC codes), this would ensure that a level playing field is maintained without one form of retailing or type of good being either controlled or privileged over another. It also avoids the categorisation issues raised earlier with respect to sub-categories such as packaged groceries, fresh fruit and vegetables and the like.

### **Levels of market concentration**

Work in the UK (Competition Commission Guidelines 2003) suggests that a combined market dominance above 25% would "normally be sufficient to raise potential concerns regarding the effects of the merger on competition" noting that lower levels of concentration may also trigger concern. In this regard it is noted that for most items reviewed by the ACCC enquiry into the competitiveness of retail prices for standard groceries concentration was above this level. In the case of the ACT, Woolworths is understood to have approximately 50% of the market, whilst Coles has approximately 19%. Aldi, whilst growing, remains a small player. IGA stores are not a chain or franchise but instead represent independent operators utilising a single marketing banner. Other entrants such as Tesco are also considering taking up positions in Australia.

Implementation of a 25% floorspace dominance test within specified regional markets would ensure that new supermarket opportunities within regional and subregional markets were largely taken up by small players or new entrants. Given the network of supermarkets existing, this should ensure additional competition. This approach was supported by the ACCC review. (ACCC Inquiry into Competitiveness of Retail Prices for Standard Groceries page 241).

### **Market concentration and the neighbourhood centres**

A floorspace dominance test could also operate in terms of neighbourhood centres, both in terms of overall size and the composition of centres.

With respect to the overall size of a neighbourhood centre, the ideal size should be focused around the optimisation of walkability. Research varies with respect to the optimum size of a walkable neighbourhood centre. Recent research undertaken by Macroplan for the Master Grocers Association (submission to the Victorian retail review 2009) suggested a limit of approximately 1700 m<sup>2</sup>. Work carried out by Wakefield Planning in Ballarat and also for Eurobodalla Shire in NSW suggests centres can extend in size up to 2000-2500 m<sup>2</sup> depending upon the overall balance between district and local retailing. These sizes are consistent with a centre spacing of approximately 1.6 km, which facilitates an 800 m "ped-shed" - typically used as the walking radius for rail transit.

Floorspace dominance tests could also operate in terms of centre composition. In order to ensure a good retail "mix" and to ensure competition within the neighbourhood centres, floorspace dominance tests be used to manage the overall floor space of a single retailer. Wakefield Planning conducted work in Eurobodalla Shire in NSW which established that effectively functioning centres needed at least 30% floor space as supermarket but not more than 50%. This suggests that supermarkets in the range of 850-1250 m<sup>2</sup> are appropriate to anchor neighbourhood centres. Supermarkets below approximately 550 m<sup>2</sup> are likely to be ineffective as anchors.

### ***The floorspace dominance test as an assessment "trigger"***

A key aspect in utilising a floorspace dominance test is to ensure that there is a robust mechanism for reviewing developments that trigger the floorspace dominance test to determine whether they have a significant net community benefit. This avoids the floorspace dominance test being seen as an arbitrary control (such as a cap would be) but instead sees it as providing "trigger levels" beyond which specific justification in terms of net community benefit needs to be provided for new development.

Based on the UK work, a 25% figure would be a starting point that it is prima facie anti competitive, for the reasons outlined in the ACCC Inquiry. On this basis there is a need for a test that assesses the development in terms of overall community net benefit noting the evidence from the ACCC Inquiry that a lack of competition produces community disbenefit.

### ***Economic modeling and a net community benefit test***

There has been concern expressed regarding the traditional measures of assessing retail impact. For example, the NSW Land and Environment Court challenged the use of the dominant "Marketinfo" model with respect to its ability to appropriately assess the spatial impacts of retail change (Eurobodalla Shire vs Jetset Properties). Similar concerns have been expressed in the United Kingdom with respect to the overall quality of assessment of retail impact. It is important, therefore, to ensure that robust and defensible criteria are utilised to assess the net community benefit, and that these are capable of objective review.

Getting the "net community benefit" test correct is therefore the most important element of reviewing developments that exceed the floorspace dominance test. The net community benefit test needs to examine both tangible and intangible aspects of the proposal. It needs to recognise that centres are much more than the provision of retailing, but that they represent social and administrative hubs as well. Net community benefit tests need to include (but are not limited to) the following:

- Will there be a net benefit in terms of the total value of land and commercial development in the relevant retail catchment?
- Will there be any loss of capital value within a specific retail sector, so that the retail sector would be restricted in its ability to raise capital and compete?
- Will there be a net reduction in overall car travel?
- Will there be an increase in local accessibility to frequently used goods and services?
- Will the rezoning integrate with and complement an existing centre or, if a new centre, will it not significantly undermine the viability of an existing centre?
- What other social implications are there of the development?
- What are the implications for net employment?
- Will the development facilitate competition within the relevant retail catchment?

## Summary

To further the aims of National Competition Policy the town planning system can be utilised to improve the competitive environment with respect to retailing. This can operate through a floorspace dominance test set at 25% of the floorspace owned or managed by a single retail operator within both regional catchments and within the ACT overall.

A floorspace dominance test can also be applied at the neighbourhood level to avoid dominance of a neighbourhood centre by a single retailer, and also to maintain neighbourhood centres at an appropriate scale to maximise walkability.

A floorspace dominance tests can be used as a “trigger” for the conduct of rigorous and comprehensive net community benefit tests where proposals come forward outside the trigger levels.

Finally, it is noted that the leasehold system within the ACT provides an alternative mechanism for implementing floorspace dominance controls other than the conventional land use planning system.