PICK N PAY'S RESPONSE TO UNITRADE MANAGEMENT SERVICES

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INTRODUCTION

1. Pursuant to the Grocery Retail Market Inquiry's email of 4 October 2016, we set out herein our client, Pick n Pay's, response to the submission made to the GRMI by Unitrade Management Services ("UMS").

2. We understand from UMS's submission that it is *"a voluntary buying association"* and that it regards itself as *"a substantial player in the grocery retail market"*.[1] In other parts of its submission, UMS styles itself as a *"voluntary trading association"*.[2]

3. The UMS submission is unfortunately characterised by numerous allegations and contentions which are unsupported by any facts or evidence. In addition, UMS has made a number of proposals, ostensibly in order to address the so-called anti-competitive practices which it has alleged to exist in the retail grocery industry. It is respectfully submitted that these proposals are either contrary to the relevant provisions of the Competition Act or are likely to be found to be unconstitutional if they were ever implemented. We will elaborate on these issues in more detail below.

THE NATURE OF THE COMPLAINT

4. In essence, UMS contends that the major corporate retailers are dominant firms, which *"engage in anti-competitive practices"*.[3] UMS seeks to expand on this general proposition with reference to a number of specific features of the market which it contends are anti-competitive:

5. First, UMS contends that the so-called *"buying power"* of the big five supermarket chains manifests itself through the so-called *"waterbed effect"*.[4] UMS explains that the so-called waterbed effect means that certain large buyers are able to negotiate excessively low prices with suppliers, which have the effect of rendering these suppliers unprofitable over this portion of sales. According to the so-called waterbed theory, as a means to recoup the margins lost to the dominant buyer/s,

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[1] Paragraph 2, page 3 of the UMS submission.
[2] Paragraph 2, page 5.
[3] Paragraph 2, page 6.
[4] Paragraph 3.1, page 7.

the relevant suppliers are forced to raise prices to smaller buyers to levels that would not have existed absent the negotiation power of the dominant buyer/s.[5]

6. This alleged application of the waterbed theory is not supported by any facts or evidence. Indeed, later on in their submission, UMS suggests that the inquiry should assess the prices that are offered to independents in order "*to ascertain if there is in fact a waterbed effect in the absence of any clear volume based discounts*".[6] It is clear that UMS does not in fact have any factual evidence to support its allegations in this regard. It is respectfully submitted that, from a competition law perspective, there is no issue with large retailers being able to secure discounts or rebates in relation to large volume purchases. This is a generally accepted practice worldwide and is important to, and has a direct impact on, consumer welfare. UMS's theory about the so-called "*waterbed effect*" is, as currently articulated, nothing more than a theoretical proposition without any factual underpinning. UMS has not presented any evidence which would suggest that suppliers are selling goods to the large retail chain stores on an unprofitable basis or that the very same suppliers have raised prices to smaller buyers in order to compensate for losses incurred in sales to large retail chain stores. Nor is there any evidence to suggest that the large retail chains are in fact dominant. The prior submission by Pick n Pay demonstrates that Pick n Pay could not be regarded as dominant.

7 Second, UMS contends that there is a lack of support by suppliers/manufacturers for independents, particularly in relation to loyalty programmes. By contrast they suggest that such support is provided to the big five retailers. In particular, they suggest that manufacturers pay corporate chains to promote their products and to participate in new store openings, whereas independents have to pay suppliers/manufacturers for the same services.[7] Once again, no evidence is put forward to support these contentions and these statements are simply bald assertions without any evidential basis.

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[5] Footnote 9, page 7.
[6] Paragraph 4, page 10.
[7] Paragraphs 3.2 and 3.3, pages 8-9

8. Third, they contend that the large corporate retail chains have "*purchasing power dominance*", that they account for 70-80% of the total grocery retail sector and that the large corporate retail stores allegedly have their own buyers groups which UMS alleges gives rise to a direct conflict of interest. As indicated in Pick n Pay's submission of 31 August 2016 to the retail grocery inquiry, it is incorrect to state that the large retail stores account for 70-80% of the retail grocery sector. In fact, the four large retail grocery stores more likely account for approximately 44.6% of the total retail grocery sector.[8] Furthermore, it is not correct that Pick n Pay has its "*own buyers groups*". Pick n Pay as the franchisor, supplies products to certain of its franchise stores, but this does not amount to a "*buyers group*". In addition, there is no factual basis for UMS's contention that the likes of Pick n Pay have "*purchasing power dominance*".

9. Fourth, UMS contends that suppliers set onerous trading terms[9] but does not specify what these onerous terms are. The UMS submission appears to be rather a complaint that independents are not able to exercise so-called "*market power*" in the same way as UMS alleges large retailers are able to do in their dealings with suppliers. Once again, these contentions are devoid of any evidence and are simply contentions in the air. While the large grocery chains may purchase significant volumes of products from suppliers, there is no indication that they are able to exercise "*market power*" as defined in the Competition Act.

10. Furthermore, UMS's submissions in this particular respect are somewhat surprising given certain of the statements on their website which are attached hereto marked "A". On its website, UMS states that "*our team of National Buyers focuses on achieving the best national deals, ensuring competitive pricing on KVIs and lines across the range and* ***negotiating preferential deals and trading terms*** *with approximately 300 suppliers.*" (Our emphasis)

11. Fifth, UMS alleges that independents are rarely offered participation in any mall developments[10]. They contend that independents have in the past been outright denied the right to participate in new malls and shopping centre developments on

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[8] Figure 20 on page 21 of Pick n Pay's submission of 31 August 2016
[9] Paragraph 3.4, page 9
[10] Paragraph 3.7, page 10

the basis that large supermarket groups bring greater foot traffic. While our client does not disagree with the proposition that large supermarket groups are likely to bring greater foot traffic to shopping malls, UMS has not put up any evidence in relation to its members attempts to engage with shopping malls in order to secure retail space within the malls. Our client is certainly not aware of any approaches by landlords to our client in respect of entry into particular shopping malls by UMS members.

UMS'S PROPOSALS TO THE GRMI

12. In its submission of 21 July 2016, UMS has made a number of proposals, which it believes will address the concerns which it has identified. We respond on behalf of our client to each of these proposals in turn below.

13. ***Proposal 1 : Similar discounts to all players***

14. UMS has proposed that similar discounts should be offered to all retail/wholesale players in circumstances where it is found that a single retailer is accountable for approximately 30% or more of a manufacturers output. We understand the proposal to mean that where a particular retailer purchases a significant proportion of a manufacturer's output, all players that purchase from that particular supplier should obtain the same discount, irrespective of the size of their purchase from the manufacturer concerned. UMS does not advance any factual or legal justification for this proposal. It does not indicate why this proposal is warranted either from a factual or economic perspective, nor does it suggest why this proposal would be in keeping with the relevant provisions of the Competition Act. While the Competition Act provides that dominant firms should not price discriminate in relation to *"equivalent transactions"*, this provision is still subject to the requirement that the price discrimination should result in a substantial prevention or lessening of competition in the relevant market. Accordingly, the mere fact that a particular retailer purchases a large proportion of a particular manufacturer's output does not in and of itself give rise to issues of price discrimination. In order to ground an actionable case of price discrimination, it would have to be demonstrated that the differential pricing *"incorporating rebates"* applied in relation to equivalent transactions and resulted in a substantial lessening of

competition. This does not appear to be the case because, in fact, the large grocery retailers compete with each other downstream and are therefore required to compete with each other to secure the best possible prices from their suppliers, which also results in a benefit to consumers. In addition, it is suggested that where one purchaser buys a significant volume of product from a particular manufacturer and another purchaser buys significantly lower volumes, these transactions are unlikely to be *"equivalent"* in nature, let alone result in a substantial lessening of competition.

15. ***Proposal 2 : Divestiture of supermarkets***

16. In relation to shopping mall leases, UMS has proposed that *"major developers should be at least 5km from a large independent"*[11]. In addition, UMS has proposed that where *"a large supermarket group has more than 35% market share in a certain locality, the supermarket could be forced to divest or sell so as to encourage diversity in the market place"*.[12] First, it is unclear what UMS means with its reference to *"major developers"*. If it is intended to refer to major retail grocery chains, then there does not appear to be any economic or legal basis for the suggestion that there should be *"at least 5km"* distance from a large independent. Our understanding is that the rationale underpinning the Competition Act is in fact to stimulate and encourage competition between the likes of retailers. We do not understand there to be any basis for suggesting that there should be artificial barriers to competition. It would be somewhat ironic in the context of a competition inquiry to suggest that the inquiry panel should actively make recommendations which are designed to stifle and limit competition. Furthermore, there is no basis in the Competition Act for the suggestion that, if a supermarket group had more than 35% market share in a particular locality, it should be forced to divest of a store or stores in that locality. This would not only be contrary to the provisions of the Competition Act, and contrary to certain previous *dicta* articulated by the Competition Tribunal[13], but

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[11] Paragraph 3.6, page 11

[12] Paragraph 3.6, page 11

[13] See Distillers Corporation SA Limited and Stellenbosch Farmers Winery Group Limited Case number : 08LMFeb02 paragraph 36 at page 9. *"...we cannot us the provisions of the Competition Act to turn the clock back, to redeem, ex post facto, the sins of the past. We are, regrettably, obliged to take the structure of the industry as we find it and, in merger proceedings at least, to limit our interventions to those transactions that result in a substantial lessening of competition."*

would also be unconstitutional given the fact that it would effectively amount to an arbitrary deprivation of property.

17. *Proposal 3 : A complete phase out of exclusive leases in shopping malls*

18. At one point in UMS's submissions there is a suggestion that the GRMI should perhaps consider *"a complete phase out of exclusive leases in shopping malls…"*[14]. However, UMS then immediately qualifies this proposal by indicating that *"the economic dynamics in the sector…..may make long leases desirable in some cases"* and goes on to propose that economic analysis should be undertaken to identify a *"term limit"* for exclusive leases, which would apply to those cases *"where exclusive leases are desirable"*[15]. They also propose that any exclusive leases that are currently in place should be subject to a phase out period.[16]

19. UMS's proposals in this regard appear to be muddled. On the one hand, they seem to be suggesting that all exclusive leases in shopping malls should be phased out irrespective of whether they apply in a retail grocery context or not. On the other hand they seem to suggest that exclusive leases may be desirable in certain instances, although they do not clearly indicate what the criteria would be for such leases to be regarded as *"desirable"*. In summary, it appears as if their proposals in this regard are poorly articulated, mutually inconsistent and without any clear indication of the criteria that should be applied in determining when a long-term lease agreement would be regarded as *"desirable"*.

20. *Proposal 4 : Quota systems*

21. Finally, UMS proposes that the inquiry should consider *"the implementation of a quota system in order to govern the level of ownership in various localities and store formats by the corporate supermarket chains."*[17] UMS appears to be suggesting a form of output regulation which is outside the remit of the competition authorities. The UMS submission does not explain how the mechanics of this proposed quota system would operate, nor do they explain the economic and legal rationale for this proposal. In keeping with our previous

[14] Para 3.7, page 11
[15] Para 3.7, pages 11-12
[16] Para 3.7, page 12
[17] Para 3.7, page 12

submissions in this regard, it is suggested that the implementation of so-called *"quota systems"* is inherently anti-competitive and is the very antithesis of what the Competition Act seeks to achieve. Indeed, we would suggest that a quota system would be tantamount to a form of market allocation or market division which is outright prohibited in terms of section 4(1)(b)(ii) of the Competition Act and constitutes a criminal offence since 1 May 2016.

22. Furthermore, the proposal relating to the implementation of quota systems is also likely to be unconstitutional on the basis that it could infringe a number of rights including the freedom of trade as well as the right not to suffer an arbitrary deprivation of property.

CONCLUSION

23. In conclusion, it is respectfully submitted that much of UMS's submission is devoid of any evidence or credible economic or legal theory to support its propositions. Indeed, a number of its proposals appear to be not only contrary to the relevant provisions of the Competition Act, but are also likely to be found to be unconstitutional in a number of respects if they were ever to be implemented.

"A"

Unitrade Management Services Pty (Ltd)

National Products and Services

National Marketing National Merchandise National Finance National IT

Our team of National Buyers focuses on achieving the best national deals, ensuring competitive pricing on KVIs and lines across the range and negotiating preferential deals and trading terms with approximately 300 suppliers.

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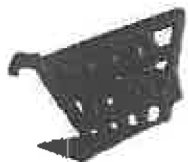
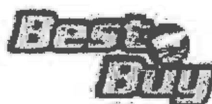


BIGGER SAVINGS
BETTER LIVING



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