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Mr Mogau Aphane/Mr Ruan Maré
Fresh Produce Market Inquiry
Competition Commission of South Africa

30 July 2024

Dear Mr Aphane and Mr Maré

Fresh Produce Market Inquiry - Provisional Report

1. Introduction

- 1.1 Thank you for taking the time to meet with us virtually on Thursday, 24 July 2024.
- 1.2 This letter has been prepared in the spirit of cooperation and the information contained herein is provided on a confidential basis. We trust that the information we have provided will assist the Fresh Produce Market Enquiry (**FPMI**) where it appears there is an incomplete or inaccurate understanding of the operations of Starke Ayres, as well as Starke Ayres' pricing. We have also included further context and information to assist the FPMI with its inquiry.
- 1.3 As a point of departure, and has been noted previously, Starke Ayres' position is that it disagrees with what is set out at *inter alia* clause 8.2.13 (numbered paragraphs 1221, 1222 and 1223) of the FPMI's provisional report (**Provisional Report**).
- 1.4 What will be demonstrated is that Starke Ayres operates within a competitive environment and the true costs incurred by it in producing its seed varieties is much higher than what appears in the Provisional Report.
- 1.5 We have set out in this letter, those factors that must be considered in any assessment whether Starke Ayres', or any similar seed production company for that matter, is pricing its products excessively.
- 1.6 Plainly, Starke Ayres is not excessively pricing its products.

2. Starke Ayres' Participation and Market Shares

- 2.1 The seed market in South Africa is a highly competitive market with a number of market participants. Given the nature of horticulture, farmers will only procure products (in this case seeds) that are cost effective and meet their product specification requirements.
- 2.2 The market shares set out in the Provisional Report are apparently determined with reference to information sourced from the South African National Seed Organisation (**SANSOR**).

- 2.3 The Provisional Report records, at numbered paragraph 918 that Starke Ayres is the biggest firm in the market for horticultural seeds. It records the following in respect of specific species:
- (a) At numbered paragraph 919 – Starke Ayres is the biggest supplier of cabbage;
 - (b) At numbered paragraph 920 – Starke Ayres and Sakata are the biggest carrot seed suppliers, where there top four suppliers have a combined market share of 85%;
 - (c) At numbered paragraph 921 – Starke Ayres is one of the top four biggest suppliers of tomato seeds, which collectively have a market share of 70%;
 - (d) At numbered paragraph 922 – Starke Ayres has the second highest market share in respect of onion seeds, where the top four suppliers have a collective market share of 79%; and
 - (e) At numbered paragraph 923 – Starke Ayres is not a major player in the spinach seed market.
- 2.4 Starke Ayres' position is that this is not reflective of the South African market. Amongst other things, the seed purchases of ZZ2, the biggest tomato grower in South Africa, are not included in the market share calculations. ZZ2 purchases its tomato seeds from foreign seed suppliers. If regard is had to seed supply to ZZ2, Starke Ayres' market share would be reduced.
- 2.5 What ought to be considered further is that within species, there exist different varieties. Purchasing farmers will select specific varieties, which may have vastly different price points, to suit their specific requirements.

3. Additional Pricing Considerations

- 3.1 Clause 6.4.2.2 (numbered paragraphs 924 and 925) of the Provisional Report describes "*price dynamics in the seed industry*". While the pricing principles referenced in these paragraphs are generally the principles taken into consideration when determining the price of seeds, they omit several important considerations to be factored in for seed production firms such as Starke Ayres.
- 3.2 In addition to the obvious elements of a 'cost price' of the production of seed (including cleaning of the produced seed, quality control, pathology testing, seed treatment and packaging), various additional costs must be factored into the calculation of a 'mark-up' to land on the true production cost. Without factoring in these additional costs, an inaccurate assessment of the seed production economics would be made. These additional costs include: Research and Development Costs, Commercialisation Costs and several other costs as explained below.
- 3.3 Research and Development Costs
- (a)

I

(b) [Redacted]

(c) [Redacted]

(d) [Redacted]

[Redacted]

[Redacted]

[Redacted]

[Redacted]

[Redacted]

[Redacted]

[Redacted]

(b)

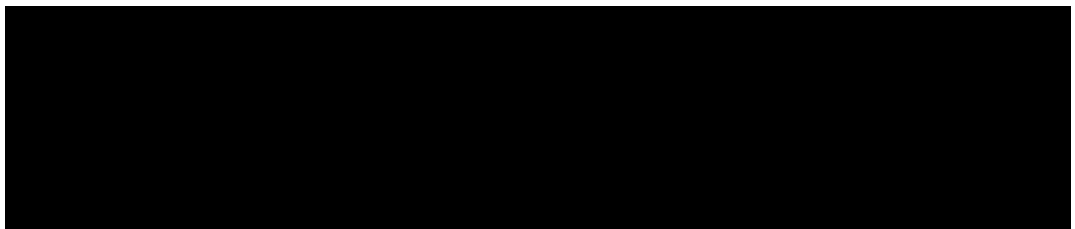


(c) Only once there is certainty that the product is suitable for the market, will the parent seeds be planted with contracted growers to produce the hybrid seed. It is only at this point that the costs in the production of that seed are allocated to the specific seed that is to be sold, and all of the operating and infrastructure related costs required prior to this point are therefore not included in the costs of the seed that has been provided to the Commission.

3.5 Other Costs

(a) Given the potential for a production failure of any one variety as a result of the agricultural risk involved, Starke Ayres targets a holding of 18 months' worth of stock to ensure that farmer customers have availability, and therefore will be able to have a crop. Outside of the substantial investment that is therefore required in this 'working capital', there are additionally the associated costs of the required infrastructure (including warehouses, cold rooms, backup power amongst others).

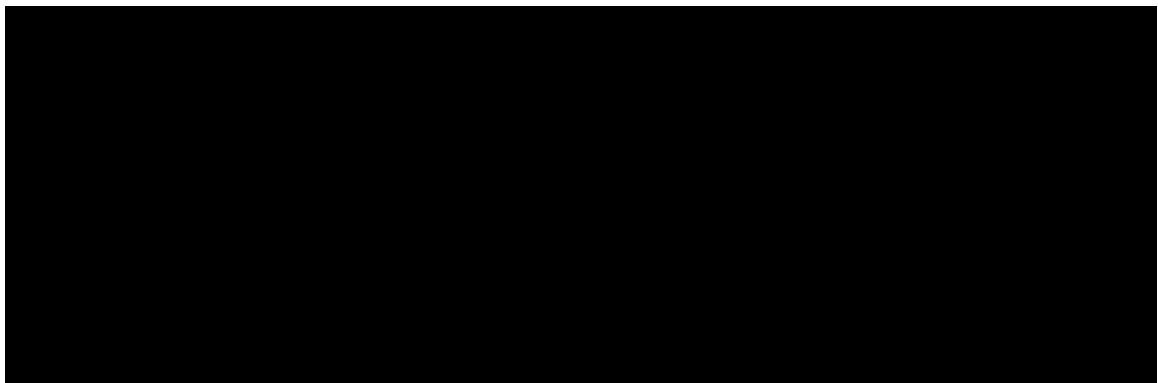
(b)



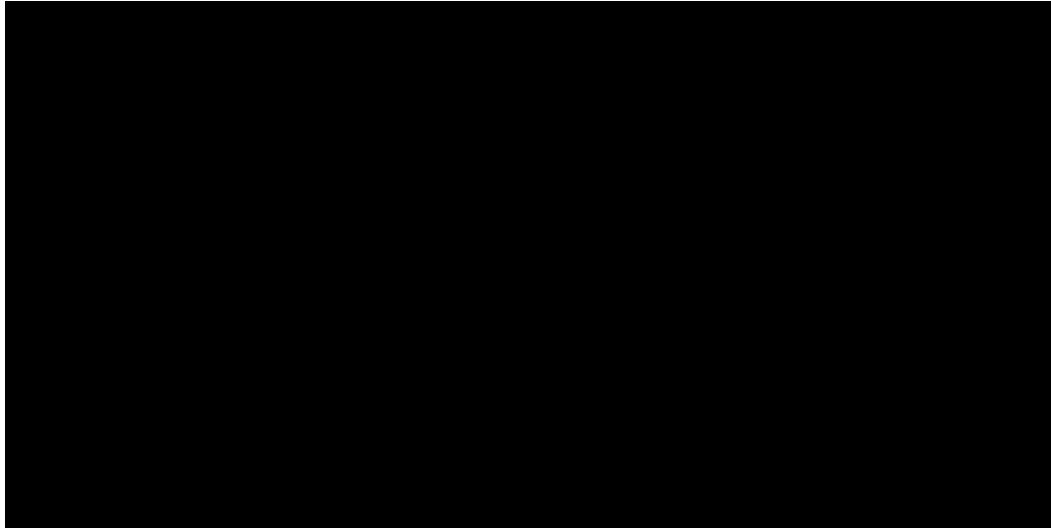
3.6 These additional costs must be funded in some way, failing which the entire business operation of Starke Ayres (and Plennegy) would be untenable. Accordingly, to arrive at a true cost of production of any variety of seed, these additional costs ought to be factored into the calculation.

3.7 Put differently, most of what may be reflected as (and on the face of it appear to be) a markup / or gross profit on seed production, is used to fund these additional costs. These costs are inextricably linked to the production of seed across the board.


3.8



3.9 Further information over the period 2018-2022:



4. Local Production and Import

- 4.1 The Provisional Report, at clause 6.4.2.2 (numbered paragraph 924), notes a concern regarding the lack of local (South African) companies with established research and breeding capabilities to meet the needs of local farms.
- 4.2 Starke Ayres is one of approximately five seed suppliers that has local breeder programmes. Several of the firms listed in **Table 53** of the Provisional Report as having breeding programmes do not breed in South Africa.
- 4.3 These are and will continue to be long term objectives of Starke Ayres, given that it can take more than ten years to develop a seed variety to the point where it can be sold commercially.
- 4.4 In numbered paragraph 929 of the Provisional Report, with reference to the markups set out in **Table 57**, it is recorded that Starke Ayres' explanation for its markups was that *"while most competitors in South Africa rely on importing seeds from international companies worldwide, Starke Ayres stands apart, [in] that, they are the only vegetable seed company that not only breeds new varieties but also produces the majority of their seeds in South Africa"*.
- 4.5 This statement is correct in respect of Starke Ayres' seed production across all of its seed varieties. The increased costs pertaining to the production of seeds that are produced in South Africa impacts the cost of all of its seed products, including those that are imported.
- 4.6 It has never been suggested that Starke Ayres locally produces all of its seeds that are sold in South Africa (including those identified in the Provisional Report).
- 4.7 
- 4.8 Given the focus on local production, and as noted in numbered paragraph 930 of the Provisional Report, substantial investment has been made, and will continue to be made, in breeding programs, production teams and specialised equipment. This substantial investment has the result of increased costs across the board, in respect of all seeds sold by Starke Ayres.

4.9 We noted in paragraph 6 of our letter of 8 July 2024, that in respect of tomatoes, cabbage and spinach, Starke Ayres imports seed, meaning that in addition to the additional costs referred to above there is reliance on external factors that cannot be controlled.

5. Other considerations

Other considerations that are important for the purposes of the inquiry, include:

5.1 Starke Ayres has a significant number of seed varieties within species, which it offers to purchasing farmers are different price points.

(a)

(b)

5.2 Star

5.3 Were Starke Ayres to lower its prices, which the economics do not support, it will place other seed producers, which cannot charge lower prices, at a significant competitive disadvantage.

6. Conclusion

6.1 In conclusion, Starke Ayres disputes the conclusions in the Provisional Report regarding excessive pricing, notably the records at clause 8.2.13 (numbered paragraphs 1221, 1222 and 1223) of the Provisional Report.

6.2 The varietal prices, determined in a competitive market, are not excessive given inter alia, the various costs involved, much of which are unique to a seed production company involved in the breeding and production of hybrid seed.

6.3 To the extent that reliance is made on what appears to be a gross '*markup*', Starke Ayres' position is that is an inappropriate measure of profitability.

6.4 We trust that the information provided herein will assist the FPMI with its inquiry, and we are confident that after completing its investigations, the FPMI will come to a finding that the prices charged by Starke Ayres are fair and reasonable.

Yours sincerely

Frikkie Bam
Managing Director: National Operations
Starke Ayres (Pty) Ltd