

Chapter 2

The proposed acquisition

Background

2.1 Metcash is Australia's largest wholesaling and distribution company, servicing over 2500 independent supermarkets and grocery stores. Metcash describes itself as the 'third force' in the Australian grocery retailing market.¹

2.2 Franklins is a discount supermarket chain that sells packaged groceries and perishables in metropolitan and rural stores throughout New South Wales. The current Franklins brand was established in 2001 after being purchased by South African retail company, Pick n Pay Retailers (Pty) Limited.²

2.3 In June 2010, Metcash entered into an agreement with Pick n Pay to acquire for \$215 million the shares of Interfrank Group Holdings Pty Ltd, which owns the Franklins supermarket chain. This agreement included the purchase of 77 corporate stores and supply to eight franchised stores. Metcash announced that, post-acquisition, it planned to sell the corporate stores to IGA retailers.

2.4 At the time of the announcement, Metcash Chief Executive Mr Andrew Reitzer noted that the Franklins acquisition would increase the company's share of supply to retailers in the New South Wales grocery market from 11 per cent to 17 per cent.³

The ACCC's review

2.5 On 29 July 2010, the ACCC commenced a public review of the proposed acquisition under its informal review process.⁴

2.6 On 22 September 2010, the ACCC released a "Statement of Issues" document which outlined the ACCC's preliminary competition concerns with the proposed

1 Metcash, 'About Metcash', <http://www.metcash.com/index.cfm?objectid=AE7C0400-A339-11DE-A93A0024E81F7375> (accessed 27 November 2010).

2 Franklins, 'About us', <http://www.franklins.com.au/home/inner.asp?pageID=6&mainID=0> (accessed 27 November 2010).

3 Metcash, 'ASX announcement: Metcash Acquires Franklins Supermarket Chain In NSW', 1 July 2010, <http://www.asx.com.au/asxpdf/20100701/pdf/31r3gmgg8wksn8.pdf> (accessed 7 February 2011).

4 The ACCC's informal clearance process enables merger parties to obtain the ACCC's view on whether it will seek an injunction to stop a merger from proceeding. Merger parties are not legally required to notify the ACCC of a merger or acquisition and can therefore proceed without seeking an informal review, formal clearance or authorisation. However, the ACCC can still examine the acquisition and take legal action.

acquisition. Consultation with interested parties on the matters raised in the Statement of Issues was conducted with submissions required by 19 August 2010.

2.7 On 17 November 2010, the ACCC announced it would oppose Metcash's proposed acquisition of the Franklins supermarket business.

2.8 In its statement announcing its opposition to the proposed acquisition, the ACCC expressed concern that the proposed acquisition 'is likely to result in a substantial lessening of competition through the removal of Metcash's closest and only genuine competitor for the wholesale supply of packaged groceries in NSW'. The ACCC also noted that its investigation had indicated that the large supermarket chains only provide an indirect and imperfect competitive constraint on Metcash at the wholesale level.⁵

2.9 In addition, the ACCC indicated that it was aware of other parties that were interested in acquiring the Franklins supermarket chain, and that these bids were unlikely to raise the same competition concerns as Metcash's.⁶

Basis of the ACCC's decision

2.10 Section 50 of the *Competition and Consumer Act 2010*⁷ prohibits acquisitions that would have the effect, or likely effect, of substantially lessening competition in a substantial market in Australia. Section 50(3) provides a non-exhaustive list of factors which must be taken into account when assessing whether a merger would be likely to substantially lessen competition. The ACCC's *Merger Guidelines 2008* also provides guidance on the ACCC's approach when reviewing and analysing acquisitions.

2.11 Compared to that held by the major supermarkets, the relatively small market share that the independent supermarket retailers would still possess if the acquisition was allowed was noted in the evidence received by the committee. Master Grocers Australia argued:

By allowing the sale to Metcash the ACCC would create a stronger and sustainable opposition to the dominance of the chain stores in NSW which would enhance competition rather than hinder it. At the present time the dominant power in the marketplace in NSW rests with Coles and Woolworths and it is estimated that between them they control 80% of the market. If Metcash had been permitted to purchase the Franklins business from Pick n' Pay, then the NSW market share increase for the independent supermarket sector would be only 17%.

5 Australian Competition and Consumer Commission, 'ACCC to oppose Metcash proposed acquisition of Franklins supermarkets', *Media Release 250/10*, 17 November 2010.

6 Australian Competition and Consumer Commission, 'ACCC to oppose Metcash proposed acquisition of Franklins supermarkets', *Media Release 250/10*, 17 November 2010.

7 On 1 January 2011 the *Trade Practices Act 1974* was renamed the Competition and Consumer Act.

Whilst this percentage appears to be relatively low, it is nevertheless a significant increase in the level of competition that independent supermarkets can provide in the market place and in particular one that will inevitably provide benefits to consumers. It is a fallacious argument to suggest that the acquisition by Metcash will hinder competition; surely any market share increase for independent supermarkets will ultimately be beneficial to the community.⁸

2.12 The National Association of Retail Grocers of Australia (NARGA) submitted that, if the acquisition went ahead, the resulting increase in market share held by the independent grocery retailers in New South Wales would lead to:

...increased marketing spend, a stronger negotiating position with suppliers and the ability to do better and more frequent deals for promotions which would benefit consumers.⁹

2.13 However, the consumer organisation Choice submitted that the acquisition of Franklins' distribution business by Metcash would create an effective monopoly in the wholesale market for groceries in New South Wales. Choice argued that there appeared to be 'no prospect' of either Coles or Woolworths supplying wholesale services to their retail competitors, and noted that:

In Australia, the competing model to the integrated supermarket chain has been a combination of centralised distribution through one company, delivering grocery items under agreements (usually exclusive agreements) to independent and franchised retail stores. This is the model operated by Metcash nationally (through its IGA>D distribution business) and by others such as SPAR in some states. Franklins operated a hybrid model that combined a number of its own retail stores with some independently owned outlets.¹⁰

Alternative sale process

2.14 The issue of what is likely to happen to the Franklins supermarkets in the event that Metcash's proposed acquisition does not go ahead was raised in submissions received by the committee and has been noted by the ACCC.

2.15 NARGA submitted that in their view it was unlikely that another credible buyer for the Franklins business would emerge as:

a new buyer of the “whole” [Franklins business] would be acquiring a business which has already proven unsustainable, even with the expertise, experience and substantial resources of Pick n Pay behind it. Franklins made a profit in only one year since it began operating as a Pick n Pay

8 Master Grocers Australia, *Submission 6*, p. 3.

9 National Association of Retail Grocers of Australia, *Submission 2*, p. 2.

10 Choice, *Submission 5*, p. 7.

subsidiary. Any purchase “in part” would be likely merely to compound the problems such a buyer would face.¹¹

2.16 Further, NARGA argued that if the proposed acquisition was successfully blocked, because Pick n Pay has indicated that it would sell its corporate stores by tender in the event that its agreement with Metcash does not proceed, this would see:

Woolworths and Coles cherry-pick the best of the stores and increase their market dominance in the world’s most concentrated retail grocery market.¹²

2.17 However this was downplayed by the ACCC. In the ACCC's 17 November 2010 statement announcing its opposition to the transaction the ACCC Chairman, Mr Graeme Samuel AC, was quoted as stating:

It should be clearly understood that today's decision by the ACCC does not in any way mean that the big supermarket chains can come in and acquire their choice of Franklins stores. To the contrary, any proposed acquisition will be subject to the scrutiny of the ACCC, and as part of this process the ACCC will be mindful that other parties, who appear to raise no competition concerns, have expressed strong interest in acquiring the entire Franklins business and continuing to provide strong competition in wholesaling to independent supermarkets.¹³

11 National Association of Retail Grocers of Australia, *Submission 2*, p. 4.

12 National Association of Retail Grocers of Australia, *Submission 2*, p. 2.

13 Australian Competition and Consumer Commission, 'ACCC to oppose Metcash proposed acquisition of Franklins supermarkets', *Media Release 250/10*, 17 November 2010.