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JOINT COMMITTEE ON THE RETAILING SECTOR

Reference: Industry concentration in the Australian retailing sector

FRIDAY, 13 AUGUST 1999

CANBERRA

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JOINT SELECT COMMITTEE ON THE RETAILING SECTOR

Friday, 13 August 1999

Members: Mr Baird *(Chair)*, Mr Jenkins *(Deputy Chair)*, Senators Boswell, Ferris, Forshaw, Murray and Schacht and Mrs Elson, Mr Fitzgibbon and Mr Nairn

Senators and members in attendance: Senators Boswell, Forshaw, Murray and Schacht and Mr Baird, Mr Fitzgibbon, Mr Jenkins and Mr Nairn

Terms of reference for the inquiry:

Industry concentration in the Australian retailing sector

WITNESSES

Committee met at 9.09 a.m.

LOWES, Mr Jeremy Stephen, General Manager Sales and Customer Service, Coca-Cola Amatil

WAGSTAFF, Mr Alec, Corporate Affairs Manager, Australia, Coca-Cola Amatil

CHAIR—I call the committee to order and declare open this public hearing of the Joint Select Committee on the Retailing Sector. I welcome all witnesses appearing before us today. Today’s hearing in Canberra is the final one of the committee’s inquiry into industry concentration in the retailing sector before the committee reports to parliament on 30 August. I welcome back representatives from Coca-Cola, Mr Jeremy Lowes and Mr Alec Wagstaff.

The committee prefers all evidence to be given in public. However, at any particular stage you may wish to go in camera and, if that is your preference, please make a formal request to the committee and we will then consider it but with the warning that at some stage in the future the Senate may decide to make it public. That is fairly rare, but we should provide that warning. The committee has before it submission No. 314 in the transcript of evidence from your appearance before this committee on 12 July. Is there anything you wish to add or detract from that?

Mr Lowes—No.

CHAIR—I now invite you to make an opening statement. At the conclusion of your remarks we shall proceed to questions.

Mr Lowes—Thank you. We at CCA have made a conscious strategic decision not simply to sell our products to customers who then on-sell them to consumers; we have chosen to co-market our brands to consumers with our retailing trading partners to drive per capita consumption and maximise returns for all the stakeholders involved. As we stressed in our previous evidence, our growth ambitions can only be realised in partnership with our customers. We value and promote a vibrant and diverse retail sector.

A practical demonstration of the value we place in the development of the independent retailers is the investment the Coca-Cola system makes in the training of independent retailers. Over the last eight years, through our support of well over $2 million to the IGA Training Institute in Australia, the Coca-Cola system has enabled over 20,000 independent retailers and their staff to participate in the institute’s training programs. In 1998 some 4,500 retailers and their staff participated.

What we sell to our customers is not just a simple soft drink; we provide to our customers a total beverage retail solution including the right package to meet the consumer demand and thereby maximise retail profitability, delivery of product, cold drink and merchandising equipment, service of that equipment, order and inventory management, consumer research and promotional activity, et cetera.

In summary, our business success depends on the success of our customers. Therefore, we support a strong and diversified retail industry. We believe the best way to achieve our business objectives is to deal directly with our customers and to co-market our product with them. We sell our products on like terms to like customers. Those terms are determined by the cost of doing business, including the nature and level of our support and marketing investment with that customer.

CHAIR—Thank you for coming today. Last time we went through extensive questioning with your organisation, and we found it particularly interesting. Since that time I have taken particular note of how coke is marketed in various outlets, but today in particular we are at a critical stage of the committee's deliberations. I think we as a committee need to get a firmer handle on the whole process of the pricing, wholesaling, and the ultimate price. One of the factors that occurred in our deliberations around Australia was the discrepancy in price at which the average retailer is able to purchase product compared to the price at which majors are able to sell it at retail.

We talked about the 1.25 ml bottle in your case. Retailers around Australia complained constantly that the cheapest they could buy it for was $1.80 through the wholesaler but it was being sold retail for $1.30. That was commonly expressed. If your people have gone through the transcript, you would have noted how often Coca-Cola's name came up. So it is somewhat symbolic. To a certain extent you were representative of other groups last time. That is why there was not much time spent on this issue. Today we have a wider cross-section, so you have been brought back as part of that.

What I and the committee would like to zero in on is the whole process of pricing—the volume discounts, the promotional discounts, and what is eventually passed on to the retailer. What has been alleged is that the price you sell to Davids, one of the significant wholesalers or the significant wholesaler, shows all of the same discounts as applied to the majors—that includes volume, promotional discounts, et cetera—yet those discounts do not necessarily flow on. That could account for part of the discrepancy in pricing that we see around Australia. That has been alleged by various sources. Obviously, from our point of view, we want to focus on the discrepancy in pricing between what happens in the dealings with the majors and what happens in the dealings with the retailers, because their ability to compete in the marketplace is certainly impeded by the questions of pricing.

Could you explain to us what happens? Bear in mind that this is a parliamentary inquiry and misleading information is regarded as a contempt of the parliament.

Mr Lowes—Of course. I need to comment again on our approach to pricing. I cannot comment on the approach of Davids to pricing. I am not in a position to do that. But I can go through again how we approach pricing. As I said in our last evidence, our pricing is a function of the volume and the investment we make in the particular customer. The mix of those two determine the ultimate price to the customer.

So let me give you two extremes—I think that is the best way to start and then we can work back. A major food store, or a Davids food store for that matter, has large volumes. The sophistication of the customer to be able to craft with us a business plan is great. We would work with that customer to craft a business plan. We would then be able to provide trading terms to resource that business plan and that would form the basis of the pricing. In the food store segment, part of the business plan would include promotional allowances, further price reductions on certain products from time to time. Those prices would flow through to the retailer and the retailer would hopefully pass them on to the consumer.

The other extreme is tobacconists. For a small tobacconist, our investment would be more in service, cold drink equipment, merchandising equipment and signage. We would strike trading terms based on volume and the price would reflect the cost of those other investments in that business. Those two scenarios would explain the extremes of pricing.

CHAIR—From your observation, which I think is critical, do you see Davids passing on these discounts?

Mr Lowes—I cannot comment on that.

CHAIR—I believe you can, Mr Lowes.

Mr Lowes—No, I cannot. I am not privy to it.

CHAIR—So you have no idea.

Mr Lowes—I have not done the research. I have not asked the question. I do not know.

CHAIR—You must have some idea as to whether they pass on the discounts.

Mr Lowes—I would imagine they do. But I have not asked the question. Genuinely, I have not tried to get evidence of the fact. It is irrelevant really in our relationship—

CHAIR—It is not irrelevant to us.

Mr Lowes—I can understand it is not irrelevant to you. We deal with Davids as the delegated representative of the retail banner. They are empowered to work with us to craft a business plan and to negotiate support funds for that business plan on behalf of those customers. Those business plans have key deliverables and Davids work with the retailers to ensure that those deliverables are delivered in the stores. Those are our objectives. We drive the business through ensuring that those deliverables are effected in those stores.

CHAIR—So the volume discounts that apply to Coles and Woolworths and Franklins are exactly the same volume discounts that apply to Davids.

Mr Lowes—The trading terms to Coles, Woolies and Franklins are exactly the same. They include the volume discount.

CHAIR—What about the promotional discounts?

Mr Lowes—There are two elements. There are the trading terms which are a recognition of the plan. Those are the same to Coles and Woolworths and Franklins and Davids. There is promotional allowance on particular products from time to time and the amount of that promotional allowance is the same as it is across all those customers.

CHAIR—If that is the case, then don’t you think it is a little curious that we get one product with such a discrepancy? Take the 1.25 millilitre bottle of coke, for example.

Mr Lowes—I would imagine that those customers—and I do not know who they are—are not retail food banners of Davids. We do not pass on those additional promotional discounts to the non-food store banners of Davids. We have additional costs of doing business with those people. We still call on their stores. We still provide the cold drink equipment and our pricing to them reflects that.

CHAIR—It is still a big discrepancy. There is a discrepancy of 50c between what they can buy wholesale and retail. So something is happening there in the marketplace between the two. This committee has the ability to recommend transparency. Whatever might be said or not said today, we could have a situation where transparency—

Mr Lowes—I am not hiding anything from you.

CHAIR—I understand.

Mr Wagstaff—Last time we spoke Senator Boswell in particular was frustrated with the definition of ‘different Davids customer’. That example—and we do not know the exact example—

CHAIR—It is in the transcript.

Mr Wagstaff—But they did not identify the actual store.

Mr Lowes—A newsagent was indicated.

Mr Wagstaff—A tobacconist was the case. They would not buy through Davids wholesale—

CHAIR—We had evidence from more than tobacconists. We had it from a variety of stores right around Australia.

Mr Lowes—I could provide you in camera with the actual banners for whom we provide these additional promotional discounts and we would expect those banners to pass those discounts on to consumers.

CHAIR—Rather than clearing the room for that, maybe you could send a confidential note to the secretary.

Mr Lowes—I will do that.

Mr Wagstaff—And that would have the prices.

Mr NAIRN—So what you are saying is that the arrangements that you have with Davids also include who Davids supplies effectively. So your contractual arrangements with Davids actually go beyond the wholesaler: they go to the end user of the product, even though Davids, as the wholesaler, is selling the item to the retailer.

Mr Lowes—That is correct, Mr Nairn.

Mr NAIRN—Have you come to that arrangement because of the type of servicing that is provided? In the case of the IGA banner, they are not in the business of selling ice-cold cans of coke for immediate consumption; they are in the business of selling packs of coke on the shelves like Coles and Woolies.

Mr Lowes—There are two key influences. One is the investment that we have to make per case, if you like—the cost per case of serving those stores. Even though they might buy the product via the Davids distribution network, we are still making a significant investment in those stores. We would call on a Davids grocery store up to three times a week. So we send people there three times a week. That is a big investment.

Senator BOSWELL—What do you do when you see them? Do you take an order and then pass it back to Davids?

Mr Lowes—We would rotate the stock, manage their inventory levels for them, take an order, give that order to the store who then passes it on to Davids through their normal network, build their promotional displays, supply all the signage in store, supply signage outside the store in some cases. We pay for that. It is significant. There are up to three or four pieces of cold drink equipment in large independent stores and we service that cold drink equipment. It can be up to a $10,000 investment.

Mr NAIRN—It is quite a unique arrangement really when you think about it, that a supplier has a contract with a wholesaler that is tied to who the wholesaler sells to.

Mr Lowes—As I said in my introduction, our preference is to do business directly with the customer. That is why we set up a network to be able to do that. We have 1,500 sales people in the field, 250 technicians, 130,000 pieces of cold drink equipment, 400 delivery trucks and drivers. That is a core part of our strategy. But if customers elect that they want to purchase through an organisation like Davids then we give them that option. Davids customers are able to buy products from us directly at the same price that we charge Davids for the products, except for the freight difference.

Mr NAIRN—The only incentive really for them to go through Davids is because of the volume aspect.

Mr Lowes—Seventy per cent of the large ones buy through Davids and 30 per cent of them choose to buy directly from ourselves. It is their choice.

CHAIR—You told us last time that you provide fridges to the small retailers and you provide them for free and they cost $3,000 and you serve warm product through supermarkets. Last time I was in a supermarket I noticed that there were all these refrigerators with the Coca-Cola brand written at the top of them and they were stocked with

90 per cent of product from Coca-Cola. What you had told us was a special deal for the retailers you are doing exactly the same for the majors.

Mr Lowes—It is a small part of the majors business. For those products that those majors sell through those refrigerators they pay the full price; they pay the same price as the small guys for those products. That is the point I made last time about different products for different users. For those immediate consumption products at the front of those stores, Woolies would pay the same price, other than their freight arrangements, as that newsagent in Kingaroy.

Senator BOSWELL—You are saying that a store in Kingaroy can buy from your organisation at the same price as Davids can supply him.

Mr Lowes—A banner store?

Mr Wagstaff—An IGA banner.

Senator BOSWELL—Then why is there such a discrepancy?

Mr Lowes—I do not think those people you are talking about are banners. I am not sure who they were.

Mr Wagstaff—If they are, we cannot explain why there is a discrepancy.

CHAIR—If they are banner stores—and Mr Reitzer will be here soon to talk about this—why would you expect the discrepancy to be there?

Mr Lowes—I really do not know.

CHAIR—You are the director of marketing for Coca-Cola. So you have no idea what the difference would be in what the average banner group would get their product at?

Mr Lowes—I do not believe they are paying $1.59 or $1.69 or $1.80. I do not know. I have not checked it out. But I would not imagine that to be the case. You need to understand though that those low prices they quote—$1.39—are not in those stores every day of the week. Those prices are only made available for that product for that week and our price reduction on those products is only made available to those stores for that week.

CHAIR—I must go to supermarkets all in the right week then. That is all I can say.

Mr Wagstaff—There is a rolling program of promotion.

CHAIR—So I am always on a roll.

Mr Wagstaff—Somewhere along the line they will be on promotion.

Mr Lowes—In a particular week that Woolworths does not have 1.25 millilitre bottles on promotion they will pay the full price. They will obviously get their trading terms, but they will not get a further promotional price.

Senator MURRAY—Mr Lowes, are you familiar with the phrase 'channel captain'?

Mr Lowes—Yes.

Senator MURRAY—It is sometimes proximated as the price maker. Do you consider your company to be the channel captain in terms of your product or is the retailer the channel captain?

Mr Lowes—We might have a different definition of channel captain. It is certainly a core part of our business strategy to establish ourselves as the customer champion. In that sense we try to develop our business relationship with the customer.

Senator MURRAY—Let me be specific, otherwise you will give me a corporate response. A channel captain can essentially dictate how the market is going—through their advertising, their marketing, their business plans, their business strategy, their pricing strategy. They essentially call the shots. What I am asking you is: who calls the shots? Is it your company or is it the retailers or is the power distributed along the distribution chain?

Mr Lowes—Quite clearly, the retailers call the shots and more specifically so when it comes to pricing. We do not influence retail price as a point of order. However, in terms of other decisions, we bring to the table a lot of knowledge and a lot of influence. We would obviously put our case in terms of our interpretation of what is good for the retailer in very positive terms for the retailer to consider. We believe our capacity to do that exceeds that of our competitors and therefore through that we earn the position, if you like, of category champion.

Senator MURRAY—If you contend that the retailer calls the shots and therefore the retailer determines the end price, the next thing I need to know from you is: how important is that end price to you? Have you done price elasticity studies, for instance, to indicate that a reasonable movement in price matters to your total volume sales?

Mr Lowes—Every day of my life.

Senator MURRAY—What is the price elasticity for your product?

Mr Lowes—It varies in various channels. It is dramatically different by channel and dramatically different by package.

Senator MURRAY—But you describe your product overall as highly price elastic.

Mr Lowes—It is very price elastic in the food store environment when sold ambient; it is very price inelastic when sold cold in the convenience channel—totally inelastic.

Senator MURRAY—I assume it is inelastic in what is known as on-consumption environments—bars, restaurants.

Mr Lowes—Totally inelastic.

Senator MURRAY—If there were to be a forced pricing change such that no retailer could sell their product at a lower price than any retailer could buy it—that is what is happening right now; supermarkets are selling at a lower price than the cost price of ordinary retailers—what effect would that have on your sales? If the market were adjusted so there would be a more fair pricing strategy, would the constant be that your returns would drop or your volume would drop or would there be no effect on either?

Mr Lowes—This is a general statement because it is in view of the 114,000 customers; they do not all behave as one. In general, outside of the food stores, retailers will benchmark their pricing to the market around them and do not pass on better buying prices to the consumer. So in terms of them getting better buying prices whichever way, those would not be reflected to the consumer and therefore we would not get a benefit of increased sales in the elastic market.

Senator MURRAY—If no retailer could sell at a price lower than they can buy from you—I am not talking about margins here or anything—

Mr Wagstaff—That is the case of the best price that any customer in the country can purchase it for compared to the worst price, regardless of customer type.

Senator MURRAY—But we are talking about making sure that no retailer ends up buying from you at a price lower than somebody else can sell it, because you have to assume that the supermarkets want to make a margin.

Mr Wagstaff—Are we comparing supermarkets to supermarkets, because our costs differ? The environment that you are suggesting would be devastating to our company, because if we were forced to standardise our prices regardless of our costs—

Senator MURRAY—I am not forcing you to that at all. Let me give you an example. Let's assume that retailer A, with no volume at all, can buy a product from you at $2. Let's assume that retailer B, with huge volume, can buy that product from you on a volume discount basis—let's say $1.50. It would simply require the person buying at $1.50 not to sell at a lower price than $2. That would give them a margin of 50c and it would give the supermarket who has not got the volume discount no margin. You still retain a margin difference between the two.

Mr Wagstaff—It would be a tax on the consumer. In essence, that is what that would be. That would not be in our interests.

Senator MURRAY—It may not be in your interest. The accusation against the Coca-Cola company in this country is that you are manipulating the market so that the small retailer cannot fairly compete. This committee has not made a judgment, but that is the accusation before this committee. For this committee to consider ways of fixing it, it has to look at alternative means. One is to ensure, through the ACCC, that the pricing procedures you employ are fair. The other is to provide some sort of benchmark such as I have outlined to you. The committee has not come to that view. I have just given you an example of one way it could be dealt with. What happens to customers is that they go into that small supermarket and they see that the price is so much ahead of the large supermarket and they believe the small supermarket is profiteering, yet there is no margin.

Mr Wagstaff—You were not here when we gave evidence last time. In terms of that price manipulation, the key point of our business strategy is to grow our business. We can only grow sales if our customers' sales grow.

Senator MURRAY—I understand that, which is why I checked through that evidence to see if there was any discussion about price elasticity. If your product was price inelastic, price movements of a reasonable level—obviously not an extraordinary level—do not affect your volumes. I want to know from you how sensitive the price is.

Mr Wagstaff—You will see that we have two very different marketing approaches for cold drink and for ambient. One where the price is inelastic and other factors, apart from price, drive consumption—the availability of a fridge, the point of sale material, the promotion that is on at the particular time and the brand's strength. We choose to market our investment not in price through those customers but by providing them with the equipment and the material which then enables them to get a very high margin on those products.

Senator MURRAY—If the accusation of what is essentially a predatory pricing strategy were true, there is only one of two ways to correct it: either the price to the consumer goes up in which case the consumer loses out; or your price goes down and you lose out. That is why the question as to whether you are the price maker, whether you call the shots, whether you are the channel captain, whether you are conducting a predatory pricing strategy matters. If you are the culprit, you should lose out, not the consumer, not the retailers. The assumption is that any adjustment of this relationship would affect consumers and retailers detrimentally. Maybe it needs to affect you detrimentally. I make it clear that neither the committee nor I make any judgment of that sort at this stage, but those are the kinds of issues that are before us.

Mr Wagstaff—Obviously we do not predatory price. One test of that is if you looked at our public results and looked at our return on assets for the Australian business you will see that we are not drawing supernormal profits from this area.

Senator MURRAY—Are you under any investigation as an international company by the ATO on transfer pricing?

Mr Wagstaff—Not that I am aware of.

Senator MURRAY—So there is no inference that you are taking your profits other than in Australia?

Mr Wagstaff—Not that I am aware of, no.

CHAIR—The American situation is that there is one price. I am not sure what the exact name of the act is, but you know that there is that requirement. So there is one price that applies to everybody but a set scale for the volume discounts that you get and also a set scale for the promotional discounts that apply. How would you respond to that type of requirement?

Mr Lowes—It is our understanding that the net result in the US even with that structure is the same as it is in Australia. You would come to arrangements with the customers on benefits and you would have price allowances—

CHAIR—What type of benefits?

Mr Lowes—Business plan, promotional frequency, the space allocation on shelf—in America, not here. You would negotiate those kinds of benefits and they would affect the price. The prices paid in the States I believe are not all the same. The prices are a net result of the relationship between the customer and not just the product itself.

CHAIR—It seems interesting that they have that situation legislated whereas in this country anything goes.

Mr Lowes—Yes.

CHAIR—There is no transparency.

Mr Lowes—It would be worthwhile researching the American model.

CHAIR—We have been doing that.

Mr Lowes—I would like to make a point that we are very positive about the contribution we make to all retailers including the small retailers. The fact that we go about making it possible for small retailers to participate in this category to sell, to present the products in an attractive way, to present them ice-cold so that they can earn volume and very attractive margins, is something that we are particularly proud of. It is something which is in the heart of our business strategy. Ensuring that our 114,000 customers have vibrant, commercially attractive businesses with our brands is the foundation on which we stand. That may mean that certain prices in the marketplace differ on particular packages from time to time. But in the total business relationship of the right products for the right customer, the support we provide to ensure that that customer can make a good profit is fundamental to what we do.

Senator MURRAY—To my memory, no witness has made allegations of unprofessionalism. Your company is very highly regarded as a professional marketing company. All the allegations are about your pricing practices.

CHAIR—No-one would doubt your marketing credentials.

Mr Lowes—Including pricing.

Mr Wagstaff—From the evidence I have seen, the complaints have been very selective about particular packages. They have not been general. In fact we have checked on prices for some of those customers and, without wishing to draw the veracity of their complaints, some of their complaints are not consistent with what our own record shows as to what those customers do.

Senator SCHACHT—So they have lied to us, have they?

Mr Wagstaff—That would be up to them to answer. There is definitely a conflict in some of those cases.

Senator SCHACHT—You will provide us with the evidence where they got it wrong, will you?

Mr Wagstaff—Yes. I am happy to do that, definitely.

Senator SCHACHT—I presume in a company that is as efficient as Coca-Cola Amatil you have a code of practice in a manual that you provide to all your managers at various levels.

Mr Lowes—Yes, we do.

Mr Wagstaff—We have two. We have a code of practice in terms of actual behaviour and we have a trade practices compliance booklet.

Senator SCHACHT—Could you provide a copy of the code of practice in relation to behaviour to the committee in confidence?

Mr Wagstaff—It is a public document.

Senator SCHACHT—Does that deal with the issues that Senator Murray has been raising about pricing?

Mr Wagstaff—I do not believe it deals with it directly.

Senator SCHACHT—So it basically says you have to wear a nice clean suit.

Mr Wagstaff—No.

Senator SCHACHT—So is it a bit more than that?

Mr Wagstaff—It says that you cannot accept gifts, you cannot provide lavish entertainment, you have to comply with the laws of the country. It is a code of conduct that covers our operations internationally, not just in Australia.

Senator SCHACHT—You have a pecuniary interest declaration form, do you?

Mr Wagstaff—Not a declaration of interest, although you do have to reveal if you are a director of an outside company and seek permission from the company to hold that directorship.

Senator SCHACHT—But you cannot take more than $500 a year in free chocolates or free beer or something.

Mr Wagstaff—There is not a dollar limit, but there is a definition of what is considered to be lavish.

Senator SCHACHT—So it does not deal with the price; it deals with what we might call ethical issues. Has anyone in the last five years been sacked from Coca-Cola for breaking that code?

Mr Wagstaff—Yes.

Senator SCHACHT—Five or 500?

Mr Wagstaff—I would have to check. It would be closer to five than 500.

Senator SCHACHT—If it were 500, I am sure you would be on the front page of the newspaper. The trade practices compliance manual is drafted by your lawyers. Is it a user friendly document in that it says, 'This is the act. These are the provisions. Be careful because this is the one that will get you into strife if you do certain things'?

Mr Wagstaff—I believe it does. It focuses on those areas of the act which directly relate to our business. I am happy to provide that to you. We provided that to Professor Fels last week.

Senator SCHACHT—Is that a public document?

Mr Wagstaff—I am happy to make it public.

Senator SCHACHT—It is not written in the way of how to minimise problems, how to get around the Trade Practices Act?

Mr Wagstaff—No. It is part of a compliance program.

Senator SCHACHT—You are telling me it is a dead straight document, that it is down the line: if you do this, you will end up in strife or the company will end up in strife.

Mr Wagstaff—I believe so. In fact it says along the lines of: 'Don't do this because this would breach the law.' We provided that to the ACCC in the last few weeks.

Senator SCHACHT—How long have you had that document?

Mr Wagstaff—A number of years. I am not sure of the exact time.

Senator SCHACHT—Is that the first time the ACCC have seen it?

Mr Wagstaff—I do not know.

Senator SCHACHT—Why did you provide it to the ACCC, other than being nice?

Mr Wagstaff—Following Professor Fels's media comments about potential complaints—

Senator SCHACHT—On the GST?

Mr Wagstaff—No, on predatory behaviour, anti-competitive behaviour, our managing director visited Professor Fels two weeks ago to find out exactly what the issue was. Professor Fels indicated at that time that they had received some complaints. They had not reached any decision as to whether there was cause for investigation but they were looking into it. At the meeting we took the opportunity to table that document.

Senator SCHACHT—Were they complaints about Coca-Cola?

Mr Wagstaff—Yes. It was in the *Australian Financial Review* two weeks ago.

Mr Lowes—From competitors, not from traders.

Senator SCHACHT—It would not be from your allies. So they were from Pepsi or Schweppes or something like that. Their complaint was that, because of the size you have in the market, you are influencing the market in an anti-competitive way.

Mr Wagstaff—From Professor Fels's statements, they arose out of the ACCC's investigation into the proposed merger between Cadbury Schweppes and Coca-Cola in Australia.

Senator SCHACHT—So obviously it was not Cadbury Schweppes then because you are trying to take them over. So it is down to Pepsi, is it?

Mr Wagstaff—Ask Professor Fels.

Senator SCHACHT—Is that the first time your chief executive volunteered to see Professor Fels?

Mr Wagstaff—Yes, definitely.

Senator SCHACHT—Since the changes went through to the Trade Practices Act in 1991, nearly a decade ago, is that the first time your chief executive has felt it necessary to go and talk to the ACCC?

Mr Wagstaff—I believe so. The ACCC have written to us on a small number of occasions when they have received specific complaints. We have responded to them. This is over the last five or six years. In each case we have satisfied the ACCC that there has been no breach of the legislation and no further action has been taken.

Senator SCHACHT—Does Coca-Cola Amatil have any view or any concern that the Trade Practices Act may be amended to strengthen the provisions against anti-competitive behaviour?

Mr Wagstaff—We do not have a view. It is very hard to comment on something until there is a specific proposal.

Senator SCHACHT—You have seen some of the suggestions that have been floating around in this inquiry.

Mr Wagstaff—We have not particularly focused—

Senator SCHACHT—So none of them particularly send you off to drink hemlock or something?

Mr Wagstaff—I could not say that without having a close examination. We have not seen them at this stage.

CHAIR—Are you implying by your answer before that that for small retailers there are significant advantages belonging to a banner group? Is that part of the answer: small retailers being gathered up in a grouping so that the benefits can be passed on?

Mr Lowes—I think that is true. I think a well run, disciplined banner able to bargain collectively and efficiently deliver market practices in accordance with a business plan, if you like, could be a real advantage for small retailers. In fact some do benefit from being part of a banner such as Davids.

CHAIR—So, in your opinion, you are not aware of whether organisations such as Davids, despite being the largest wholesaler in the country, are passing on the volume discounts and the promotional discounts?

Mr Lowes—I am not. I have not asked the question and I am not aware.

CHAIR—What is your view?

Mr Lowes—I imagine they would.

CHAIR—You imagine they would—based on prices?

Mr Lowes—I have not given the matter a lot of thought, to be honest. I cannot see why they would not. They are there to work on behalf of their customers. They need to earn the privilege of those customers belonging to their banners. They have to deliver to those customers, otherwise those customers will go and get their supply from another wholesaler.

CHAIR—That is what they are saying.

Mr Wagstaff—Or direct from us.

Mr Lowes—They can buy direct from us tomorrow. In fact we would prefer that and Davids know that.

Senator SCHACHT—Do you have a relationship with people whom we would describe as franchisees: you are the franchisor and they are the franchisees?

Mr Lowes—People who might own Hungry Jacks, for example?

Mr Wagstaff—No. We have subcontractors.

Senator SCHACHT—That is different.

Mr Wagstaff—But not franchisors or franchisees, no.

Senator SCHACHT—So you have never seen it necessary to sign on to the franchising code?

Mr Wagstaff—No.

CHAIR—Thank you. I am sorry it has been an extended process. Obviously it has been important, particularly because Coca-Cola was mentioned so many times during the inquiry as a flag company where problems were occurring. If you could provide us with the additional information—

Mr Lowes—We will do that.

CHAIR—Thank you for coming once more to Canberra.

Mr Lowes—Thank you for the opportunity.

[9.55 a.m.]

MOFFATT, Mr Roderick, Sales Director, Kraft Foods Ltd

CHAIR—I welcome Mr Rod Moffatt. The committee prefers all evidence to be given in public. However, you may at any time request that your evidence or part of your evidence be given in camera. You can make a request to the committee at any time and that will be considered with the warning that at some stage that may be made public by order of the Senate. I also remind witnesses that the giving of false or misleading evidence may constitute a contempt of parliament. The committee does not have a submission before it, but I invite you to make an opening statement and then we will proceed to questions.

Mr Moffatt—I am the Sales Director of Kraft Foods Ltd and have the responsibility of managing our business with all sectors of the trade. I am assisting this inquiry on behalf of Kraft Foods Ltd. I commenced working with Kraft 30 years ago and have been Sales Director for Kraft Foods Australia for over five years and have maintained strong linkages with all channels in the Australian marketplace.

Kraft Foods manufactures, markets and sells a variety of food products for both local and overseas consumption. These include various cheeses, mayonnaise, spreads, salad dressings, canned meals, prepacked dinners, snack foods, coffee and confectionary. Kraft Foods competes with various other suppliers in relation to its range of products. Kraft has a view that strong trade partnerships with all customers is an integral element to ensure that our products are available to consumers and commercial end users in optimal condition.

We operate with the philosophy that our selling environment to all customers should be open and transparent and that there is a level playing field of opportunity for all customers. Our principles are: any customer may purchase any Kraft product upon meeting the criteria of our pricing policy; any customer is entitled to the applicable quantity discounts relating to order size; the discounts applicable to parcel buyers reflect the savings achieved in the economies of scale between the various order sizes; and Kraft uses our customer distribution networks to efficiently distribute goods to individual stores.

Trading terms are in place with each customer and these are based on customer performance criteria which are negotiated with each trade customer in a competitive environment. We believe our trading terms and promotional support meets the needs of each of our customers and the expectations of our consumers. We have developed pricing and allowance protocols which are open to all customers who have the opportunity to purchase products on the same terms upon meeting our purchase requirements.

Our belief is that competition is healthy for all concerned and that extending the same opportunities to all customers will allow the most efficient environment for marketers and retailers to operate in. Ultimately, we believe it is the consumer who decides how, what and where they purchase. We support a market environment that is open and able to meet the changing dynamics and needs of our consumers. I am happy to answer any questions the committee has. As you mentioned, Mr Chairman, to the extent your questions traverse our specific trading terms and terms negotiated with specific customers, I would ask that these questions and my answers be taken in camera.

CHAIR—Thank you for coming here today. To all of you in the room who represent the companies we have chosen, please do not feel that there is any reason that you should be paranoid about being here. It is because of your size in the retail market; it is not because you are multinationals or any of those other factors. It was seen that you represent the large companies who have a significant role. Because this is about retail concentration—and we had spoken to two of the majors before—it was thought that we should widen it in terms of understanding the wholesale area. I know that there are several of you who come here today with some reluctance, but it is about assisting us who are not marketers, who are not out there in the retail sector, to have a better understanding of the market, and who best to be able to tell us something about this than the people who are directly involved in a significant way in the marketplace. That is what it is about. I would like to pass on to my colleague, Senator Schacht.

Senator SCHACHT—Is Kraft Australia a totally foreign owned company operating in Australia?

Mr Moffatt—That is correct.

Senator SCHACHT—On the share registers in America or Europe are there any Australian shareholders of significance?

Mr Moffatt—I really cannot answer that question. I do not have the knowledge.

Senator SCHACHT—Can you give us the dimension of your manufacturing capacity in Australia, separate from distribution and retailing?

Mr Moffatt—When you say ‘manufacturing’—

Senator SCHACHT—Do you manufacture your own cheese or do you buy it? Do you manufacture mayonnaise? Do you manufacture a whole range of products that go under your brand name in the supermarket?

Mr Moffatt—In terms of everything we sell in the retail market, we manufacture that all ourselves and it is made here in Australia. In terms of our food service business, I would say that at a guess about 90 per cent of our business would be manufactured by ourselves.

Senator SCHACHT—How many people do you employ on the manufacturing side of Kraft? I do not want the figure to the last five, but roughly?

Mr Moffatt—Approximately 1,500.

Senator SCHACHT—How many suppliers do you have direct contact with on the manufacturing side?

Mr Moffatt—I really cannot answer that question. I am not trying to evade it. It is just that I am on the sales side, not on the manufacturing side.

Senator SCHACHT—Please take that on notice. This is a retail inquiry, but another issue keeps circulating around. Your major success and your being a major supplier of the product mean that, in the manufacturing side, you are therefore a dominating force with the small suppliers, whether they are farmers producing milk or whatever. That is another area where, on the other side, small farmers, small business people who are supplying parts of the product for processing complain they are in a weaker position. So, though this is retail, I would appreciate it if you could provide us with some information in that area.

Mr Moffatt—We can do that.

CHAIR—Perhaps I could bring you back to the question that we were pursuing with Coca-Cola in terms of the pricing. Do you wish to clear the room now? The most significant aspect for us is in terms of the pricing relationship you have with individual retailers, with the majors and so on, and how it works. Perhaps at this point you will want to go into camera.

Mr Moffatt—If we talk in principle, I am happy to talk in the open room. If we are talking specifics, I really would like to go into camera.

CHAIR—We will cover the principle first and then clear the room while you talk of specifics, because this is the area we want to get into.

Mr Moffatt—In principle, when you look at the price that we charge, all customers have the same opportunity to purchase at the same price if they meet our pricing policy requirements.

CHAIR—When you say ‘pricing requirements’, what are they?

Mr Moffatt—It means that, if they meet a certain parcel requirement, they will get a discount for a larger order.

CHAIR—Straight volume?

Mr Moffatt—Yes.

CHAIR—Nothing else?

Mr Moffatt—No.

CHAIR—No promotional discount?

Mr Moffatt—That is in our trading terms. There are two aspects: there is the price that is charged, which is determined by our pricing policy; and then we have trading terms with each account. The two are separate.

Senator SCHACHT—Is the promotional support in the individual trading terms?

Mr Moffatt—Yes.

CHAIR—It is a general principle—just as we have heard from Proctor and Gamble—that anybody, if they have sufficient volume, can get discount. There is no special deal with Woolworths or Coles.

Mr Moffatt—That is correct.

Senator BOSWELL—We have trading terms and we have a buying structure saying that, if you buy X, you will get that price. But with the trading terms, it comes down to settlement discounts, promotional discounts, advertising allowances and television promotions. Are they all the same?

Mr Moffatt—A lot of elements make up the trading terms. When you take them all through to the bottom line, they are basically the same with all customers.

Senator BOSWELL—So, if Davids were to buy a truckload of cheese, Coles were to buy a truckload of cheese and Woolworths were to buy a truckload of cheese and you netted it all down—you took out all your trading terms, all your settlement discounts, all your promotional discounts—they would all come out at the same bottom line.

Mr Moffatt—There are two separate elements to this: one is the volume discount, and one is the trading terms.

CHAIR—Is it trading terms you want to speak of in camera?

Mr Moffatt—Yes.

Senator SCHACHT—But just on the principle, following on from Senator Boswell's question: take Coles, Woolworths and Davids with those truckloads of cheese turning up. If in the overall marketing Coles were to sell more of your cheese than Woolworths, they would, with the principle, get a bigger discount because they had a bigger volume.

Mr Moffatt—No, that is not quite the way it is. You get the largest discount when you buy 750 cases of our product. So, if you buy 750, you will get the largest discount; if you buy 2,750, you will get the same percentage discount.

CHAIR—We discussed before just in general principle the American requirements of a standard price to everyone and the discounts being set out clearly so that everyone knows. Do you support that type of approach?

Mr Moffatt—Yes, I do. In fact, that is the way we operate. Everybody knows what discounts are available for what quantity they are going to buy.

Senator SCHACHT—For volume.

Mr Moffatt—For volume, yes.

CHAIR—Is it all set out according to the promotional discounts as well, or is this where we get into the trading terms?

Mr Moffatt—No. Promotional discounts are based on performance and they are negotiated.

Mr FITZGIBBON—On the volume discounts, this is the highest threshold. What is the lowest threshold for the discounts?

Mr Moffatt—We have a minimum delivery of 20 cases; that is minimum delivery. But we have a threshold of mixed.

Mr FITZGIBBON—That is the minimum delivery, but what is the first threshold for a discount? The upper threshold was 750.

Mr Moffatt—Yes. Between nought and 49 cases is what we call the list price, and between 50 and 100 you get a five per cent discount

Mr FITZGIBBON—Can you give us some idea of how many items that is? I am trying to assess what size store you would need to be before you would be in a position to lock into that, or to take advantage of that. You mention 49 cases. How many are in a case?

Senator SCHACHT—That is a lot of cheese.

Mr Moffatt—No, we sell a lot of products. A small store could easily do 50 cases of Kraft product.

Senator SCHACHT—A week, a fortnight, a month?

Mr Moffatt—A week—because we have such a wide range.

Mr FITZGIBBON—Without going into camera, can you give us some idea about the differential between the thresholds? For the 49 threshold, you might get a 10 per cent discount. Then, once you go through the 750 threshold, you might be talking about 20 per cent or 30 per cent.

Mr Moffatt—Twenty to 50 is list-based price; 50 to 100 is five per cent; 100 to 200 is 10; 200 to 750 is 12½; and the best buy cuts in at 750, which is 13½.

Senator BOSWELL—Would you sell to any stores direct? You probably only have four or five customers. You would not direct deliver to stores, would you?

Mr Moffatt—Ninety-nine per cent of our business is through the majors. There are a few around that over the years have stayed there for one reason or another.

CHAIR—When you say ‘majors’, how do you define majors?

Mr Moffatt—We are talking of Coles, Bi-Lo, Woolworths, Franklins, Davids, FAL, AIW—in the retail sector. As I said in my opening statement, we are very heavily reliant on the distribution network.

Senator MURRAY—That surely lessens your pricing flexibility and freedom. In contrast with Coca-Cola who say that they have 114,000 customers, you have 10 or 20. That must mean that you are more captive to their pricing decisions than Coca-Cola would be. You must be more dependent upon the pricing decisions of those majors that you describe in terms of the end price of your product. In the sense that we were discussing earlier, you cannot be a channel captain in the same sense as Coca-Cola surely.

Mr Moffatt—If I understood what you were talking about with 'channel captain', that does not apply to us.

Senator MURRAY—In other words, those majors call the shots to you rather than the other way around in terms of the end price.

Mr Moffatt—That is correct. We are concerned about the price at which we sell to each of the major accounts. What happens after that is their call.

Senator SCHACHT—Can I ask: 99 per cent direct to the major retailers—

Mr Moffatt—Wholesalers.

Senator BOSWELL—No, wholesalers and retailers. Davids is a wholesaler.

Mr NAIRN—But they are selling to Coles and Woolworths in their wholesaling capacity.

Senator SCHACHT—Yes.

Mr Moffatt—Yes.

Senator SCHACHT—Take the Narrandera independently owned supermarket. How many of those sorts of people do you sell direct to, or do they have to go through the wholesalers? Can they ring up and ask to buy 50 cases off you?

Mr Moffatt—Theoretically they could. But, in practical terms, they would be much better served to go through the wholesaler—firstly, because we probably do not go there, to start with, so we do not know his business. Then, in terms of getting the product there, how do we get the stuff to Narrandera? It is just the practicalities of us servicing Narrandera. So the answer is yes, but not in practical terms.

CHAIR—Do you think there is potential for a lot of these small retailers, in terms of the Banner groups, to provide the bulk, to service them directly? We are looking at how we can assist the small retailers. Can you offer any comment on that?

Mr Moffatt—I have to say that going through the wholesalers in terms of working the promotional programs and meeting the needs of the various banners works pretty well for us. You have one port of call. That is efficient, we can do it, we have the resources to manage that. If you break that down any further, it does become more difficult. So we are saying that we are pretty comfortable with the current system.

CHAIR—I would invite our guests here this morning to have a coffee break while we go into camera. We will advise you when we have completed our in camera hearing.

Evidence was then taken in camera, but later resumed in public—

[10.35 a.m.]

ALFORD, Mr Bradley Allman, Managing Director, Nestle Australia Ltd

KELLY, Mr Peter John, General Manager Corporate Services, Nestle Australia Ltd

CHAIR—Welcome. The committee prefers all evidence to be given in public, but you may at some stage wish to go into camera if you believe there is information very sensitive to your company. As you have seen with the previous attendee, that is possible, with the only proviso being that at sometime in the future the evidence may be made public. As we advised the previous participant, that is usually pretty remote, but it does occasionally occur.

The committee does not have a submission from you before it. We do appreciate your coming today. These hearings are about us understanding more of the marketplace; how pricing operates in relation to suppliers and wholesalers, and the final impact on small retailers. We invite you to make an opening statement.

Mr Alford—As I said, I am the Managing Director of Nestle Australia, an appointment I took up 18 months ago. With me is General Manager of Corporate Services, Peter Kelly, who has been a member of our executive management team for four years and with the company for 26 years.

Nestle is one of the leading food suppliers to the retail industry in Australia and has been part of the Australian food industry for more than 90 years. Unlike many of our competitors, we have an extensive range of products, which includes beverages, culinary, confectionary, ice-cream, chilled dairy, milk modifiers, pet foods and others. Some of the products within our range are category leaders, and others are number four or five in their category. This portfolio of products includes more than 1,000 stock keeping units—or SKUs, as we call them—which span 160 categories in the grocery business. This adds up to a complex business operation.

As this inquiry is focusing on the ability of retailers to compete fairly in the retail sector, I will briefly outline our position in this regard. We endeavour to offer consumers as many opportunities as possible to purchase a broad array of products, which is one of the keys to our success. Consequently, we work closely with all of our customer and treat them equitably to achieve this outcome. The existence of a vibrant, competitive retail sector in Australia is clearly in the long-term interest of Nestle. I will endeavour to answer any questions you have relating to our operations.

CHAIR—Thank you very much. As I said before, the reason for your being chosen along with the other major food suppliers is because of your significance in the market and understanding a little bit more about the way the market operates.

Senator SCHACHT—Does Nestle have any Australian shareholders?

Mr Alford—We are not traded on the Australian share market, but we would have, I assume, Australian shareholders—

Senator SCHACHT—Through international investments.

Mr Alford—Yes, but I do not know that for a fact.

Senator SCHACHT—I grew up on a dairy farm and, to me, Nestle was always a Swiss company. Is that still basically the case?

Mr Alford—We are based in Switzerland, yes.

Senator SCHACHT—But what about the shareholding?

Mr Alford—I do not know the break-out of the shareholder percentages, but I would assume that the Swiss shareholders have the majority of the shares.

Senator BOSWELL—Has the company been in Australia for 90 years?

Mr Alford—Yes.

Senator BOSWELL—Has it always been a Swiss company?

Mr Alford—Yes.

Senator BOSWELL—I would assume that you sell for four or five, maybe seven or eight customers basically. You do not go to individuals.

Mr Alford—Correct; in the grocery business, yes.

Senator BOSWELL—The discounts and trading terms that are offered to the majors: are they offered to the 'Davids' that service the independents?

Mr Alford—Yes. If they all meet the same performance criteria, they all get the same price.

Senator BOSWELL—That is based on volume?

Mr Alford—Volume is one of the terms of trade, yes. But they all get the same line discount.

Senator BOSWELL—Davids would buy at the same volume as Coles or Woolworths?

Mr Alford—They buy the same volume increments; they do not buy the same amount of products from us. In other words, Coles and Woolworths would have a bigger per cent of our total business.

Senator BOSWELL—So they meet the maximum discount requirements?

Mr Alford—Yes. One thing you need to understand about it are our volume breaks, because of all the categories that we are in, are different by category. So confectionary and pet food have different volume breaks—

Senator BOSWELL—What pet food brand do you sell?

Mr Alford—Friskies pet food. So it would be GoCat on the cat side and Lucky Dog on the dog side, primarily.

Senator BOSWELL—Do you aggregate all your products up and say 'You must buy 1,000 cartons,' or do you say 'You have to buy 1,000 cartons of dog food, 1,000 cartons of x-y-z'?

Mr Alford—We mix primarily. But there are instances where we will sell a full truck of dog foods.

Senator BOSWELL—We may have to go into camera for this, but you may care to answer it. Do not feel that you have to answer it if you would prefer to go into camera. Are there any discrepancies in the trading terms between Woolworths, Coles, Franklins and Davids?

Mr Alford—If you want to get into the specifics to that, I would like to go into camera. But in terms of the top level, the trading terms are the same if they can meet the performance criteria—for example, with the volume, or paying within whatever the credit terms require.

Mr NAIRN—So 'like customer, like conditions'.

Mr Alford—Correct.

Senator MURRAY—Within this inquiry are a couple of main propositions put particularly by the independent supermarkets. One is that the increase in market share, market power by major retailers to their detriment is the result of a retail market growth strategy and, therefore, it has nothing to do with the suppliers. The second proposition is that there are some suppliers who contribute to undue market power by their pricing and marketing practices. That is essentially the allegation against people like Cocacola. If I understood your answer to Senator Boswell correctly, you are like Kraft: you have relatively few customers—

Mr Alford—On the grocery side, yes.

Senator MURRAY—I would assume from that, therefore, you are not, in my terminology, the channel captain, you are not calling the shots; the end price and the nature of the market is more determined by retail activity supported by your brand marketing than by your activity in terms of price.

Mr Alford—In that context, yes, we are more similar to Kraft. Our customer is either the big wholesaler or the big chain account.

Senator MURRAY—Is there any sense—and bearing in mind the nature of answers in this format—where you would describe your pricing and marketing strategies as unfair or discriminatory or predatory with respect to major groups?

Mr Alford—No.

Senator MURRAY—That is, including wholesalers and small independents.

Mr Alford—No. It is in our best interests to have as many points of distribution as possible to get this wider area of products that we have out. So my answer would be no.

Senator MURRAY—Is it in your interests as a marketer for there to be a healthy and large independent grocery sector?

Mr Alford—Yes.

Senator MURRAY—Why?

Mr Alford—More places to sell our product.

Senator MURRAY—Any other reasons?

Mr Alford—That would be the primary reason to me. As I said, we have a number of products here. The more places that I can get them in front of the consumer, the better chance I have to sell.

Senator MURRAY—But is Australia—and you are an international company, and I would expect by your accent that you have international experience—

Mr Alford—Yes.

Senator MURRAY—Is Australia unusual in the limited number of customers available to you and, therefore, much harder in terms of the pricing pressure those may just put you under?

Mr Alford—I am an American, first of all, so you know the background. The industry structure is dramatically different; as you say, there are many more customers that we deal with in the US. But, in terms of the ability to work with our customer group here, I do not find it any more or less onerous than I was used to in the US. You have to remember that I have not worked in the retail sector in the US for 10 years.

Senator MURRAY—I am familiar with the retail sector in the US to a considerable degree. Let me put it formally to you: Australia exhibits the characteristics of a oligopolistic retail sector. 'Oligopoly' implies that the ability of that oligopoly to manage price and terms of trade is far more pronounced than in a more open and more competitive market. The consequence of that should be greater pressure on manufacturers and marketing suppliers—unless, like Coca-Cola Amatil they have this huge bypassing ability because of their distributional decisions. Is that a true reflection of this market? Do you find, as a company, that your margins, your return on investment, is leaner and harder because of the pressure of the majors in this oligopoly here?

Mr Alford—Our return on investment here is lower than in the US. But I do not find that as a function of our relationship with our trade customers.

Senator SCHACHT—But you would say that, wouldn't you. That is not something you would want to have on the record. If you have an oligopoly at work, you have to be very cautious about what you say if they are your major customers.

Mr Alford—Basically, if you want to look at what the dimensions are, the difference in terms of the return on invested capital for us, in the primary areas we are able to manufacture our products cheaper in the US.

Senator BOSWELL—I think what Senator Murray is saying is: if you had 500 customers in America and you dropped one, you could live with it. But if you dropped Coles here, it would be a disaster.

Mr Alford—You would be talking to someone else next year.

Senator BOSWELL—So you are really beholden to those four customers that are left in the market.

Mr Alford—Absolutely.

Senator SCHACHT—Therefore, even at a public hearing like this where you are under privilege and you can say what you like and can't get sued, I do not blame you for being very cautious in saying anything about that relationship—because, if one of them nails you, you have gone.

Mr Alford—But the other senator's question was: do I find it more onerous dealing with the trade here than I did in the US? The answer to that is no—whether that is because a number of my customers are in here or not. But the one thing I have found is that our customers here understand that they have a mutually dependent relationship for to us bring products to the marketplace and to help them grow their business. So the working relationship I have found here—to answer the question—is not more onerous.

Senator SCHACHT—Is that because, on the supply side, you have such a big sector of supply that they cannot live without you?

Mr Alford—I would say that is part of the mutual relationship.

Senator SCHACHT—Though there are the different brand names and the different company structures, there is still a structure of vertical integration here: just as you might get chopped if you lost Woolworths, the manager of Woolworths might get chopped if he lost you.

Mr Alford—You would have to ask Woolworths about that. But I would say that that is a fair representation of the relationship.

Senator MURRAY—So the strength of your brand is your protection.

Mr Alford—Correct.

Senator MURRAY—But if you were in the commodity market, a commodity supplier, you could be skinned alive, couldn’t you, in that relationship—if you were just a supplier of unbranded meat or sugar?

Mr Alford—I have never competed in that category, so I do not know. I have been with this company my entire life.

Senator MURRAY—But as somebody with formal training, implicitly that has sense, hasn’t it?

Mr Alford—True. That is why we invest so much money in building our brands and advertising our products.

Senator SCHACHT—What percentages of the market do you have with the products that you produce?

Mr Alford—There is a lot of them.

Senator SCHACHT—Just take it on notice and come back to us.

Mr Alford—Okay.

CHAIR—Can you give us a couple of representative ones?

Mr Alford—Nescafe would be our biggest brand; it is 50 per cent of the soluble coffee market. That is roast and ground, and there are other kinds of coffee. But Nescafe would be our biggest brand name. Probably the second biggest one would be Maggi Two Minute Noodles. That has around 60 per cent of what we call simmer noodles or two-minute noodles. KitKat would be our biggest confectionary product; it has a seven share in the chocolate bar category.

Senator SCHACHT—It has a seven per cent share?

Mr Alford—Yes, seven. The biggest pet food brand would probably be Go-Cat. We can send you the market share data, if you like.

Mr NAIRN—It makes Davids, with its critical mass and as a major player, quite important as well. We are talking about getting down to just a few customers. But, taking that argument further along the oligopoly line, if the size of Davids reduces further and further—which some people say will occur—with Coles and Woolworths getting bigger and bigger, that really is not in your interests because the less of those sorts of equal players, the more likelihood that the boot goes on the other foot. Then you would be found responding only to the customer rather than with this two-way street that tends to occur now. Would that be true?

Mr Alford—That would be true.

Mr NAIRN—So it is certainly in your interests that an independent wholesaler like Davids remains of a reasonable critical mass size.

Mr Alford—That would be true.

Mr NAIRN—With some of your chocolate products and things that go into convenience stores and so on, is your circumstance similar to Coca-Cola's? With KitKats and such things as refrigerated items in small stores, are you feeding those stores directly? Are there two different pricing structures for those ready-to-eat cold chocolates?

Mr Alford—They just go through a different wholesaling operation.

Mr NAIRN—So you work it through the wholesaling end; you do not support any of the equipment or anything like that that keeps chocolates cool?

Mr Alford—Correct.

Senator BOSWELL—Does Cadbury do the same?

Mr Alford—Cadbury goes through a wholesaler also.

Senator BOSWELL—Do you have operators out there selling through the wholesalers?

Mr Alford—Correct—salespeople, yes.

Senator BOSWELL—And channelling the orders back through the wholesalers?

Mr Alford—Correct.

CHAIR—With your experience, having worked in the US, can you tell us of the Robinson-Patman act? How do you feel that act worked there, and what do you think its applicability in the Australian environment would be?

Mr Alford—It is a broad question. The Robinson-Patman act in the US, I would say, works fairly well. To relate that back to Australia: having worked for Nestle in the US, our trade philosophy is no different in the US than it is here. So, when I talk about like terms for like performance for like customers, it would be no different. There are some finetuning differences in terms of how the trading terms are set up and negotiated. But the basic trading philosophy is very similar and would be consistent with what the Robinson-Patman act tries to do in the US.

Senator MURRAY—Providing that you are playing the game, the introduction of those principles here would not affect you detrimentally, would it?

Mr Alford—No.

Senator MURRAY—It would only affect those that it would be designed to affect.

Mr Alford—That is correct.

CHAIR—So Davids has the benefit of all the discounts—volume, promotional, et cetera—that the majors have.

Mr Alford—So long as everybody performs to those criteria, yes.

CHAIR—Do you believe that these are being passed on to small retailers?

Mr Alford—I remember your asking that question earlier today. We do not monitor that, but it is my assumption that they are. We hope that they are because I want those independent retail operations to stay viable.

CHAIR—We have talked about the critical mass of small retailers in the country. I just wonder whether, with your experience of the international marketplace, you have any view on this: how do you believe that we can assist small retailers to survive and be viable in the Australian market?

Mr Alford—Adherence to fair trade would be the obvious thing. If you were to read the Robinson-Patman act, that is what they refer to as fair trading. From a regulatory standpoint, to me, that would be the biggest issue.

CHAIR—Why do you believe that we are seeing so many small retailers going out of business in Australia?

Mr Alford—I think it comes back to what the consumer is looking for. If the consumer is not shopping there, it is for some particular reason. Maybe it is the price; we talked about price with Coca-Cola. Maybe it is the offering. I am not sure. But for some reason there are not enough groceries being bought at those retail outlets to make them a viable operation.

CHAIR—Do you think there is enough re-investment by small stores?

Mr Alford—As a manufacturer, I would like to see more, because I want a viable sector out there.

CHAIR—How do you compare that with, say, small retailers in the US?

Mr Alford—Small retailers in the US are shrinking also. It is a phenomenon, and I do not know what the relationship there is.

CHAIR—Is it a worldwide phenomenon?

Mr Alford—I do not know, to be honest.

Senator SCHACHT—Does Europe have tougher laws than America, similar to what we have here with fair trading and supporting small business?

Mr Alford—I have never worked in Europe, so I do not know.

Senator BOSWELL—This Robinson-Patman act: it gives discounts for volumes.

Mr Alford—Correct.

Senator BOSWELL—Does it allow anything further in trading terms?

CHAIR—As long as they are set out, as long as they are clear. Is that right?

Mr Alford—Yes, and set out to everyone.

Senator BOSWELL—So they are set out. You have a buy for so many cases, and you go down and you get your mass discount. But then what about all the gondola ends, promotional discounts, television advertising and support?

Mr Alford—The act would not get into that detail.

Senator BOSWELL—So you can still break away and give all those other discounts.

Mr Alford—Correct.

Senator BOSWELL—That does not help small business over there. It gives a volume discount, but then—

Mr Alford—The act says that you need to give fair trading terms also, but it does not lay out the specificity of advertising or gondola ends in that degree of detail. You have to remember that it goes across all channels of trade also. So it is not just grocery; it would be washing machines, whitegoods, electrical appliances, everything.

Senator MURRAY—That act, as supported by other acts and as amended, operates on the principle that like customers should be treated alike. Is that correct?

Mr Alford—Yes.

Senator MURRAY—And, secondly, that it is the regulatory authority which will examine the detail of compliance with that act if there is a material complaint.

Mr Alford—I believe that, but I do not know it for a fact because I have never been involved there.

Senator BOSWELL—But if that is the case—and we have had some prominent manufacturers here—we are being told that, apart from Coca-Cola who market a different way, Davids are receiving basically the same volume of discounts and more or less the same discounts—as the last witness said, within half a per cent—as Coles and Woolworths. So, bringing another act in, we virtually have that act—maybe it is not in an act, but it is being enforced that way. Would you agree with that statement?

Mr Alford—That is my understanding, yes. I do not know the detail of the statutory layout here in Australia, to be honest.

Senator BOSWELL—I think I speak for the committee when I say that we believe there has to be a fourth sector out there. It puts too much pressure on manufacturers, farmers and graziers if it gets down to three retailers. But we are struggling with how we get to that position. It is my observation from listening to the previous witness and the witnesses that we have had before that we really do do that in Australia. Is that a correct observation?

Mr Alford—I would say yes, and it comes back to the point that I do not find the trading relationship that different from the US, to be honest. Whether that comes from the statutory requirements or not, I do not find it that different.

Senator BOSWELL—Can we go in camera?

CHAIR—You can ask the question and, if Mr Alford feels that he cannot answer it, it would be at your request, I believe, that we should do it.

Senator SCHACHT—I do not think my question will require in camera. You mentioned before that you hoped that the discount was passed on to the independents and so on. Have you had any evidence?

Mr Alford—No, I have none.

Senator SCHACHT—Have you had any complaints raised?

Mr Alford—Not that I know of. It has not come to my level.

Senator SCHACHT—I should have asked this question of some of our earlier witnesses, but I will ask you. In view of the fact that you have four or five major customers, what sort of contact do you have at your level as a chief executive of a major manufacturer of a product with the chief executives of the supermarket chains?

Mr Alford—I would see those individuals once or twice a year.

Senator SCHACHT—In a formal business sense?

Mr Alford—I was referring to formal contact.

Senator SCHACHT—But the weekly contact is a middle level management arrangement?

Mr Alford—Yes.

Senator SCHACHT—You are a major manufacturer. For the record, how many people do you employ in manufacturing in Australia?

Mr Alford—Three thousand.

Senator SCHACHT—How much of your product that goes on the shelves is manufactured in Australia—other than coffee, I suppose?

Mr Alford—The coffee is manufactured here.

Senator SCHACHT—You bring it in bags?

Mr Alford—We bring the beans in, but it is manufactured here. In terms of the bulk of the product—and I am guessing—90 per cent would be. We have 14 manufacturing facilities here and so the bulk of our products are manufactured here.

CHAIR—Senator Boswell, did you want to ask the question and we will see whether we have an exit from the room?

Senator BOSWELL—I just want to ask a question on trading terms.

CHAIR—Why don't you ask it and we can decide—

Senator BOSWELL—I did ask it and Mr Alford said he would prefer to give it in camera.

CHAIR—Did you say you would prefer to give it in camera or not? I do not think so.

Senator BOSWELL—I was asking on the variation in trading terms. What different trading terms would you offer?

Mr Alford—I would prefer to go in camera for that kind of detail.

Evidence was then taken in camera, but later resumed in public—

[11.30 a.m.]

GLINSKI, Mr Grant, Commercial Director, Uncle Ben's of Australia

MYERS, Mr James Kirkup, Sales and Marketing Director, Uncle Ben's of Australia

CHAIR—I welcome Mr Grant Glinski and Mr Jim Myers. Thank you for coming today, gentlemen. The committee prefers all evidence to be given in public, but at some stage you may wish to go into camera and we are happy to take that on board, if you feel the requirement to do so. I also remind witnesses that giving of false or misleading evidence may be regarded as contempt of the parliament.

The committee has a submission before it, which is now authorised for publication. I now invite you to make an opening statement and at the conclusion of your remarks we will then proceed to questions. I apologise for the length of delay. We have found some of the evidence interesting. We hope we can speed things up. It often takes longer in the earlier presentations as we get to grips with some of the issues involved. I know you had some concerns about appearing. We hope this is a user-friendly experience—not everyone would agree—but thank you for coming.

Mr Glinski—Thank you, Mr Chairman. Uncle Ben's has over the years worked hard to grow its pet food business with all our trade partners. Our trading terms and promotional agreements are uniformly available to national chains, independents, wholesalers and retailers alike and demonstrate what we believe is a fair and consistent approach.

Uncle Ben's started its business manufacturing pet food in Wodonga in 1967 and Bathurst in 1978. These plants now employ 686 and 362 associates respectively. Our national headquarters is also in Wodonga. In addition to the 1,048 directly employed by us in regional Australia, we contribute directly and extensively to local economies through our policy of procuring goods and services locally. We estimate that we generate 3,000 additional direct jobs—the majority of them in regional Australia.

Having a strong decentralised business not only has benefits in growing employment. Additionally, we contribute to the growing development and maintenance of local infrastructure. For example, we rely on local engineering firms to build our new plant and equipment; and we rely on other local firms for our graphics production, warehousing, office supplies, furniture, maintenance laundry of uniforms and so on.

We are proud to have built a strong and growing business based in country Australia. Our brands such as Pal, My Dog, Chum, Whiskas and Kit-e-Kat are household names. We are also one of the largest exporters of high value added food products from Australia, with markets in New Zealand, Japan, South Africa, Singapore, Malaysia, Taiwan, Korea, Europe, the Philippines, Thailand, the Middle East and the Netherlands. Approximately one-third of our sales come from exports, which represents about 15,000 containers—over 159,000 tonnes—per year.

This very significant export business provides secure outlets for Australian grain, beef and chicken farmers who sell to Uncle Ben’s rather than into fluctuating international commodity markets. Every can that is sold into an overseas market represents a guaranteed market for Australian steel. We estimate that another 4,000 jobs are indirectly attributed to the suppliers of our raw materials—again most of them from rural Australia.

The diverse demographic and geographic spread of pet owners creates a strong demand for similarly diverse adaptability and availability of supply points for these consumers. Uncle Ben’s has a vested interest in developing and maintaining a broad array of channels and distribution points. Uncle Ben’s believes that impartial and fair trading terms helps it in developing and maintaining these diverse channels. The very competitive nature of the market and the many sourcing options available to all participants in the distribution and consumption chain requires that our trading terms are accessible to all and do not act as barrier to entry to new or small customers.

CHAIR—Can I just ask, Mr Glinski: do you plan to read the whole of your submission?

Mr Glinski—No, I don’t. I just want to make a very important point because I think it is relevant to questions that Senator Murray asked earlier. The pet food market in Australia and overseas is very competitive. The market consists of everything that is fed to pets and includes manufactured pet food, table scraps and fresh foods. The latter two have the additional advantage of being free of 22 per cent sales tax. This relative advantage will be broadly maintained under the proposed GST regime.

We monitor the calorific value of all food fed to cats and dogs in Australia and, as you can see from the evidence we have tendered, approximately half of the calories that cats and dogs produce are from table scraps or fresh foods. In our experience, the biggest single influence on pricing of prepared pet foods is the existence of table scraps and fresh food as alternative feeding methods. I will stop at that point.

CHAIR—Thanks very much, Mr Glinski. Thank you for preparing in a short time this submission before us. I should re-emphasise the fact that the companies that were chosen were chosen because of their reputation and their involvement in the Australian marketplace. Each of the companies appearing before us today all have very fine names in the Australian marketplace, and Uncle Ben’s is amongst that group. I had the member for Indi spending some time with me yesterday outlining the success of your company and your involvement in Albury Wodonga, part of which is in his electorate.

But simply be aware that the companies that appear before us today are not under investigation per se. We are looking at the concentration of majors but, because you are significant players in the market, you can assist us in understanding how the market works. Thank you for coming and I will open for questions.

Mr NAIRN—I just want to clarify your distribution aspect. You have given us a table, which is good. What percentage of your product is divided up in these various ways? For instance, you have a link to the wholesalers, independent and chains—AIW, Coles, Woolworths, Davids, et cetera—

Mr Glinski—Correct.

Mr NAIRN—But you also have a direct link to retailers. What type of retailers are they compared with your lines going through the wholesaler/retailer end?

Mr Glinski—Almost all of our business by volume goes through the major wholesalers—Coles, Woolworths and Davids. That would be just over about 80 per cent of the volume that we sell. We have actually got about 5,000 customers. We are quite happy—if a customer meets our trading terms for volume and pricing discounts—if they want to buy directly from us; we are quite willing to do it. We provide free into store in capital cities and virtually the greater capital cities and also into major regional centres. One of the things which we have done fairly well over the last few years is to develop rural outlets through produce stores, veterinary channels and the like. So about 80 per cent actually goes through the grocery wholesalers; the rest would be spread uniformly through the smaller channels within Australia.

Mr NAIRN—And the various trading terms that you offer, like most manufacturers, are dependent on volume and other things; do you have a suite of terms?

Mr Glinski—We have provided a copy of our price list for New South Wales. It would be identical for each state, except for the fact that the state price would show some variation owing to logistics costs. For example, getting product to Perth from Bathurst or Wodonga costs a bit more than getting it into Victoria or New South Wales. We have provided an example of that. The volume discounts are uniformly applied. The payment trading terms are uniformly applied.

Mr NAIRN—What other negotiating areas—I am not asking what you might give to one or the other—what other areas are the income part of ultimately price and—

Mr Glinski—They would be consumer promotions that we would provide to outlets. Our spend in any given week or month is probably going to vary from outlet to outlet but, over the course of a year, the percentage spend we have on consumer promotions is fairly uniform by outlet.

Mr NAIRN—Do you negotiate about shelf location?

Mr Glinski—Yes, we certainly do. Obviously you pay for gondola ends to get promotions and the like but, in terms of paying for position on the shelf, we do not pay for that. We monitor very closely scanning data and velocity of turnover of line items. We like to have all of our brands blocked together, and we negotiate those things. We are able to demonstrate to pretty much most retail outlets that that is the best way of generating profit in their stores, and it seems to work.

Mr NAIRN—And all of those things are available to all of your customers?

Mr Glinski—Yes, they are.

Mr NAIRN—Just one other question: what percentage of the Uncle Ben's products sold in Australia is manufactured here?

Mr Glinski—Almost all of it. We import a very small percentage of canned fish product out of Thailand.

Mr NAIRN—You don't want to buy a cannery in Eden, by any chance? We have a deal for you.

Mr Glinski—I am afraid not. As we speak we are importing some pouch product from France. We are test marking the market in Western Australia—

CHAIR—Pouch?

Mr Glinski—It is a pouch product. It is a plastic pouch instead of a can. That is preparatory to our building facilities in Wodonga to manufacture in Australia. In fact, our capital project program is already under way to build that factory here.

Mr NAIRN—The volume of that imported product, has that stayed much the same or has it increased?

Mr Glinski—We have done our best to stop buying co-manufactured product out of Thailand. We believe that the quality that we can manufacture in our own factories is better. We have actually successively had a program to repatriate the manufacture of that back into Australia.

We can buy pilchards, sardines and the like to manufacture in Australia. Our impediment is actually getting tuna. The tuna is caught, cooked and then we buy the tuna loins. As we are talking, we are actually sourcing tuna loins from overseas. We will import those and then can them in Australia. But that is a small proportion of the product. Almost everything else is made here.

Senator BOSWELL—We have asked this question to all the people who come before us, and I think you have probably answered it already. On a volume discount, Davids buy no less than Coles, Woolworths or Franklins?

Mr Glinski—The minimum quantity we would like to sell and that fits our terms is about two pallets. The top cut-off point is 22 pallets, which is about what you would get on a standard tray truck.

Senator BOSWELL—And that is your maximum?

Mr Glinski—That is the maximum. After that you get the same percentage discount for everything that you buy.

Senator BOSWELL—What about trading terms?

Mr Glinski—Trading terms are absolutely uniformly applied. We are quite happy to supply them to anybody who comes to us and asks to buy from us. We are quite happy to provide them to you. They are completely transparent.

CHAIR—What do the trading terms include?

Mr Glinski—The trading terms you have in front of you actually tell people what price per SKU they pay for the quantities. Customers will be aware that if they pay promptly we will give people a prompt payment discount. It is fairly significant and you would be a bit of a mug not to take it. If you don't want to and you want to buy in standard 30-day trading terms, that is your prerogative. But without exception we find people taking advantage of the prompt payment discounts.

Senator SCHACHT—Mr Glinski, what percentage of the market in your business do you have amongst consumers? You have provided a table on the pet food sources but I am really interested in the market where you have competitors also selling pet food and so on. What percentage do you have of the overall pet food market?

Mr Glinski—In terms of the calories that are sold to animals, we would be about half of the calories sold to animals. So in terms of manufactured pet food we are fairly large.

Senator SCHACHT—In your dealings with the four or five majors whom you sell to, are you now big enough such that they need you as much as you need them?

Mr Glinski—We would like to believe that, yes.

Senator SCHACHT—You like to believe it, but do you think it is true?

Mr Glinski—From time to time we have intense negotiations with them about the best way of getting our brands to consumers, yes.

Senator BOSWELL—Pal would be your leading brand, I suppose.

Mr Glinski—Yes, it is. So is Whiskas on the cat side.

Senator SCHACHT—As a manufacturer—I have asked this question to others and they might duck it. You might want to duck it, too. I would not blame you in any one way. Do you have any concerns as a company on the grocery retail side that basically it is down to four companies you have to sell to in order to get your product out?

Mr Glinski—I have spent all of my working life in Australia so I have very limited international experience to draw on, although obviously I have travelled overseas to observe things. Our observation is that the more competition you have, the better the consumer is served because it ultimately forces lower prices in the marketplace. Although you might think the number of players is limited, our observation is the competition is pretty intense, which works to the advantage of the consumer.

The other thing which I might observe from the earlier discussions—I don't know if it has been used as an exemplar or just a reference point—is that we would find it quite difficult if the Australian trade used the US practice of imposing listing fees on introduction of new products. The Australian trade does not. That is a bit of a double edged sword from our point of view because, although it allows us to innovate, it actually lowers the barrier for our competitors as well. So in a sense it might encourage competition amongst manufacturers which I think probably helps the consumer, if not the manufacturer.

Senator SCHACHT—You mentioned in your submission on the manufacturing side the number of people that you employ, et cetera. Is Uncle Ben's an Australian owned company?

Mr Glinski—The company is incorporated in Australia but we are actually privately owned by an American family.

Senator SCHACHT—Was it started as an Australian company?

Mr Glinski—No, it was incorporated initially and from the outset it has been privately owned.

Senator SCHACHT—I notice you have Garry Hocking listed here in your submission rather than Whiskas. I thought you might have listed him rather than Whiskas to return the favour. People north of here would not understand the subtlety of my question.

Mr Glinski—No.

Mr NAIRN—Can I ask the same question I asked of Nestle before: the maintenance of Davids as a viable and a reasonable size critical mass wholesaler would be fairly important to you in that if that fell further greater concentration with the other three would put much more muscle back to your customer than probably currently is—

Mr Glinski—It probably would. But they are of a size now where we have to sit up and take notice of them anyway at the moment.

Mr NAIRN—That is what I mean—

Mr Glinski—It would be a matter of conjecture about how much further Davids would diminish in size before that changed it any greater than it is today.

CHAIR—Can I just ask the question that I have asked to the others: I am particularly interested in the Robinson-Patman Act—I don't know whether you are aware of how this works but it basically makes price discrimination unlawful. It has to be transparent so there is a uniform price and then the volume discounts and promotional discounts are set out and then, as you have heard from the other people here, there are other incentives that can be provided. As a major player in the market how would you see that operating?

Mr Glinski—Firstly, I might say that I am not at all familiar with the act. I am, of course, familiar with the situation in Australia.

CHAIR—It may be useful because of your US connections if you can perhaps come back to us on that fairly quickly, if you can.

Mr Glinski—We will endeavour to do so. But through my experience I would only be able to answer questions directly about Australia.

CHAIR—The reason we are asking is that—

Mr Glinski—I understand why you are asking—

CHAIR—There is an interest in applying it in Australia. That is why we want a response to the question: if such a situation applied in Australia how would you feel about it?

Mr Glinski—We would have to take that question on notice. I am not at all familiar with the act.

CHAIR—Then the question that I feel is interesting: given the importance of having a critical mass of small retailers in the country, how would you see that assistance could be given to them by a committee such as ours?

Mr Glinski—I heard you ask that question earlier. I was trying to think of what would be the most appropriate thing. It is absolutely essential to have fair trading practices in the country. For the size of our economy and the size of our population, I think it is enormously important that barriers to trade, barriers to growth and barriers to innovation do not exist and are removed.

CHAIR—In terms of fair trading and barriers, what would you outline as that being?

Mr Glinski—In our case, our experience is that the environment is fairly competitive today. I gave you one example earlier of a benefit of that competition which is that we do not get listing fees for the introduction of new products. In the world scheme we are a small player but, as you can see, we are hugely successful. We can ship stuff to the Netherlands and compete even with our sister companies in Europe with product forms that they cannot make which we can make—

CHAIR—Why is that, just out of interest?

Mr NAIRN—We are Australian.

Mr Glinski—We are actually not a high wage country, but I might point out that our wages bill is about eight per cent of our cost. We get our competitiveness through having access to extremely good quality raw material streams. So the quality of our products is extremely good. Through where we are positioned—Bathurst, as you would know, would be in the centre of the wheat growing district—we have turned a relatively small size into competitive advantage. We have extremely efficient product changeovers; we have state-of-the-art equipment; and our factories run 24 hours a day, seven days a week. We have created many economies of scale in order to compete. I am happy to say that one of the products we send to Japan, a product called Pedigree Chum, is a market leader in Japan in prepared pet food.

CHAIR—That percentage of the wage costs, how does that compare with say the Dutch manufacturing?

Mr Glinski—I don't know, I am sorry. I should be able to answer that. I am sorry I cannot. I might point out that we actually pay our people well above award rates. They work rotating shifts; they work weekends.

Senator MURRAY—Can I swing us back onto market power. This is interesting but—

CHAIR—In terms of the impediments that you see in terms of the fair market environment.

Mr Glinski—I think if you maintain that then you create an advantage. Our experience of it is that it is fair.

CHAIR—But what factors are you talking about?

Mr Glinski—I think fair access to economies of scale. Clearly, our trading terms are all about what are the relative economies of scale. If people can get access to that in a fair fashion, then they become beneficiaries and in turn consumers become beneficiaries.

CHAIR—How do we ensure that we get fair trading terms?

Mr Glinski—Transparency helps.

Senator SCHACHT—Does amending the Trade Practices Act to make it stronger guarantee that transparency?

Mr Glinski—I am not sure how you would do that but, clearly, having a good Trade Practices Act and a good regulatory environment helps.

Senator SCHACHT—It would not worry you because, on the other side as a manufacturer with many small suppliers, if the act is strengthened you might one day find a small supplier to you of wheat, meat or so on saying to you, 'Because you are such a big size of the market and you have a dominating position as a manufacturer,' that would not worry you because you have good practices in the company?

Mr Glinski—The answer is yes, we do. You asked a earlier respondent questions about ethical practices. We have an ethics course which we run. We put all of our executives through that ethics course. It would not bother us in the least. We have suppliers that we have been doing business with ever since I joined the company.

Senator SCHACHT—As I asked Coca-Cola—I should have asked the other witnesses too—and that includes briefing about the operation of the Trade Practices Act?

Mr Glinski—Yes.

Senator SCHACHT—There is a manual on that.

Mr Glinski—No we don’t have a manual on the Trade Practices Act per se but you can see from our trading terms that we review continuously to ensure that we comply with those trading terms. I am absolutely sure that we comply.

Senator SCHACHT—So in reverse—going back to the retail sector—the same ethical base from your suppliers to you, even though there are many small players and you are the dominant player, that works the same way and you are confident—

Mr Glinski—Absolutely. I am responsible for all of our purchasing and I am absolutely confident.

Senator SCHACHT—I should have asked this of the others—I am not singling you out.

CHAIR—You mentioned about barriers, are you talking about tariff barriers and things like that?

Mr Glinski—No, not tariff barriers, just barriers to innovation and barriers to the expansion of business.

CHAIR—Like?

Mr Glinski—For example, if you can fairly give people access to economies of scale, then they can grow with you. Our rural business has grown quite considerably over the last 10 years.

CHAIR—Just two last questions: one relates to the discounts that are provided to Davids, do you see these being passed on to the small retailers?

Mr Glinski—The answer is yes. We had an example of our being sideswiped by fresh meats: our growth was starting to stall; we did some analysis of where we were positioned against fresh meat and table scraps; and we thought our pricing was out of kilter. Towards the end of last year and beginning of this year we reduced our prices quite substantially and, without exception, we saw those prices passed down to the retail outlets.

CHAIR—How would you see a cap working? The NARGA group has recommended that we have a cap placed on expansion and we actually have divestment so that no one player has more than 25 per cent of the market. How would you see the impact of that being in the marketplace?

Mr Glinski—A bit beyond my ken in terms of the way the economics would work. I would see that as being highly dangerous. The reason I would see that as being dangerous is why would you carve up Australian companies to allow very large overseas firms to enter our economy? If you want to see evidence of predatory trade practices, go to France.

CHAIR—Okay.

Senator MURRAY—Mr Glinski, Senator Schacht quite rightly indicated that changes to the principles of trade practices law will have upstream as well as downstream consequences. It seems to me from the evidence we have received about the concentration of market power at the retail end that it is only detrimental to manufacturers where they do not have strong brands—sometimes these are more than one where companies such as Coca-Cola and Rothmans have an extensive own distribution, direct sales situation and where people such as yourselves have a strongly established export market so that you have, if you like, a bit of leeway.

Our interest is where the market power lies in relationship with a particular manufacturer and sector. Do you think your brands are strong enough to prevent any one of the five majors identified—that is, Coles, Woolworths, Franklins, Davids and FAL—simply delisting your brands as an exercise of pressure and getting rid of them and refusing to carry you?

Mr Glinski—Probably not in reality. I guess the evidence would be that that would be a ‘cut your nose off despite your face’ experience for them.

Senator MURRAY—But if one of them did it, and let us assume that it was 20 per cent each, just to make the maths easy, that would hurt your business greatly.

Mr Glinski—Absolutely, yes.

Senator MURRAY—That to my mind means that the power to call the shots, the channel captaincy in the terminology I have been using for the hearing today, pretty well rests with the major retailers and the major wholesalers rather than you. To give an example, I cannot imagine any of them ever contemplating delisting Coca-Cola for instance. The brand is just too big and strong.

Mr Glinski—We go through cycles of delisting line items or particular products from time to time. The retailers argue that the manufacturer has a lot of power. We are the ones who control quality, we are the ones who, to a degree, control innovation and we are the ones who do the market research with consumers to ensure that our products meet their requirements. So I think there is kind of a symbiotic relationship going on between us and the retailers. They are in physical distribution terms and in marketing distribution terms our path to the consumer, but they would see us as having a lot of power in understanding the consumer. Ultimately, what I think happens in practice is that it is the consumer who delists the product. If they are not buying it, you are losing out because you are making something that is not being bought, and it is just costing you more than it does to sell it.

Senator MURRAY—But the point to me is as follows: a manufacturer such as Coca-Cola Amatil tells us that they have 114,000 customers and are not captive by any distribution channel or by any particular player or chain. We have heard today that there are others who have below 100, maybe 10 or 12, real customers because everything is redistributed through them, and then there is someone like yourselves.

Mr Glinski—Who are in betweens, yes.

Senator MURRAY—As a principle, and it really follows the earlier question, it is surely to your advantage as a manufacturer and a brand marketer to maximise the diversity of competition and the numbers of competitors because that gives you the most opportunities to lay off your risk, so if somebody did delist you as a form of pricing pressure, for instance, or because you are not giving them as big a deal as they want to negotiate, you might be able to wear that a bit more. Isn't it the case—it might be difficult for you to answer, and you should indicate so because this is a public hearing—that those majors have very strong muscle when they are sitting across a table talking to you about your trading terms and your pricing structure?

Mr Glinski—Yes, they do. The difficulty in the question is that there was a time when you had Jewel, Flemings and a whole bunch of people where it was almost the market as you are trying to describe at the moment. Over the years what we have seen is the market coalescing to the players that there are today. I do not fully understand the economic forces driving that, and I do not really know as a consequence whether you can turn the clock back.

Senator MURRAY—Behind my question, and it is really an observation because it would be unfair to ask you to respond, is this: this committee has heard from small independent supermarkets who were prepared to say on the record that they think Coca-Cola Amatil have not behaved well in pricing terms. In terms of trade relationships, if we should call it that, I do not think there is a manufacturer who would come to this table who, even if they felt like that about one of those five majors I outlined, would say that publicly simply because the market power is too great to risk their wrath.

Therefore, we as a committee have to feel our way through the real relationship. That is why it is important to us to know whether manufacturers want and require an independent sector which has critical mass and why you would want that. The result of the alternative of a cap or some kind of trade practices restraint will be, in theory, that the majors will grow even bigger and the manufacturer will be even more at their behest than they are now.

Mr Glinski—I am really unable to comment on some of your observations. In terms of whether we are prepared to speak our mind, we are absolutely prepared to speak our mind. We have the advantage of having trading terms that are in the public domain, that are totally transparent and totally visible. That is what we do. We are quite impartial, and fearlessly impartial, about it.

Senator BOSWELL—So you would prefer more retailers out there than fewer. That is what Senator Murray is asking.

Senator MURRAY—Yes, that is what I am asking.

Mr Glinski—We would prefer to have a highly competitive retail environment, yes. Whether that would be achieved by more, I really do not know, because, in economic terms, the consumer will often benefit by having a fewer number that are highly competitive than a disparate number that do not have the economies of scale to get the same level of value to the consumer.

Senator MURRAY—But the clear argument that this committee has accepted is that if the majors continue to incrementally grow their market share by acquiring independent stores the critical mass necessary to support viable wholesalers will not be there. In other words, FAL and Davids just could not survive because there is not that critical mass.

Mr Glinski—It is possible, but I am not really competent to answer that though. I am sorry; I do not know.

Senator MURRAY—But that is the evidence that has been given to us, and we accept it.

Mr Glinski—All I can do is accept your observation.

Senator MURRAY—That lies behind our question to you as a manufacturer. If that was to happen—not that Coles, Woolworths and whatever would take over everything; it is simply that Davids and FAL could not survive any longer—would that be a major loss to you?

Mr Glinski—You are asking a hypothetical question.

Senator MURRAY—It is becoming a reality.

Mr Glinski—It would depend entirely on whether or not competition in the retail sector was reduced to the point where the consumer started to suffer.

CHAIR—We are running substantially behind. Unless there is a burning question that has to be asked, I would like to thank you for coming. I also thank you for the submission, which was produced at short notice yet first class. Thank you for coming. Thank you for your forthright views on the issue. We appreciate you being with us today.

Mr Glinski—Thank you very much.

[12.08 p.m.]

ALLARA, Mr Enzo, Chairman, Unilever Foods

TOULEMONDE, Mr Jean-Lin, Chairman, Lever Rexona

CHAIR—I welcome Mr Enzo Allara and Mr Jean-Lin Toulemonde. You have probably heard me say this before, but the committee prefers all evidence to be given in public, but if you wish to go in camera please ask the committee and we will take that on board. I also remind witnesses that the giving of false or misleading information may be regarded as a contempt of the parliament. The committee does not have a submission before it but we look forward to your presentation to us today. Thank you for coming.

Mr Allara—Thank you, Mr Chairman. I would like to start by saying that Unilever Australia has developed a rich history in manufacture and marketing with an extensive range of consumer goods for both domestic and export markets for over 100 years. We have been here for more than 100 years. We are proud of the employment and training opportunities we provide for many Australians in a thriving business, currently employing around 3,000 people in our manufacturing facilities in New South Wales, Victoria and Queensland as well as in sales, marketing and research development.

In addition, we rely heavily on local suppliers of products and services, adding to our broad contribution to the welfare of the Australian economy. We have a portfolio of global, regional and local food, home and personal care products. Some brands such as Lipton tea and Lux soap have become world leaders. Our food categories include culinary products, ice-cream, tea based beverages and spreads. Our personal care products include deodorants, hair care, household care, laundry and mass skin, personal wash and prestige products.

As an international company, we bring a wealth of knowledge and international expertise to meet the demands of our consumers and customers with high quality, safe, creative and competitive better products. To meet the aspirations of both our consumers and customers, Unilever has relied upon an efficient and competitive retailing sector and made customers of Woolworths, Coles, Franklins, Davids, AIW and FAL. We work with these customers in a cooperative way to achieve agreed business targets and objectives. This relationship relies on trust, a transparent pricing and selling environment and equal opportunity to all customers to purchase our products. Thank you.

Senator SCHACHT—To start off, I will ask the usual question to both our witnesses that I have been asking. Unilever and Lever Rexona are both part of the same global organisation. Is that correct?

Mr Allara—That is correct.

Senator SCHACHT—You are operating in Australia as foreign owned companies. Is that correct?

Mr Allara—We are organised in the Australian way, but our shareholdings are foreign owned.

Senator SCHACHT—The only Australian shareholding is through our own institutional investors who may have bought shares on the international market. Is that right?

Mr Allara—There are a few local shareholders. I am one of them.

Senator SCHACHT—Yes, I know. I wish we could have more. Mr Allara, you have listed the groups of your product. In each of those areas, what percentage of the market do you have?

Mr Allara—We are in many categories, so you need to be a bit more specific.

Senator SCHACHT—You mentioned the food sector. Can you give me an example in that area.

Mr Allara—I mentioned culinary, and culinary is a broad expanse of food categories. Let me take soup. We have about 30 per cent of soup. We have about 40 per cent of tea.

Senator SCHACHT—Mr Toulemonde, how much share does Rexona have?

Mr Toulemonde—In deodorants we would have about 60 per cent market share. In fabrics, or laundry, we have about 35 per cent market share.

Senator SCHACHT—Thank you.

Mr NAIRN—On that particular item, what percentage of your products sold in Australia are manufactured in Australia?

Mr Allara—If I take the food side first, with the exception of canned fish the majority is manufactured in Australia. In the case of tuna it is predominately manufactured here in Australia. We import small amounts of food into this country, so we are supporting a large range of local suppliers and manufacturers of raw materials, packaging materials and services.

Mr NAIRN—And in non-food areas?

Mr Toulemonde—In non-food areas about 90 per cent of our products are locally made. When I say ‘locally’, it is between Australia and New Zealand. We have two operations and we swap production between the two countries in an equal manner.

Mr NAIRN—So you treat Australia and New Zealand as one market.

Mr Allara—In total, we have seven factories employing around 2,000 people.

Mr NAIRN—I will ask similar questions to those I have asked to previous witnesses in relation to your trading terms, which, I would assume, are based on volume. What other categories do you have for negotiation with your customers that ultimately affect the price that they buy from you?

Mr Allara—Clearly, we have trading terms based on volume. Again, talking about food, we have a range of food which is frozen, chilled and dried.

Senator BOSWELL—Which brands do you have?

Mr Allara—In chilled, we have margarine, for example. We have Flora, Miracle and those sorts of things. You have probably tried our new margarine product, I hope, in more recent times. Depending on the categories, we have a different set of trading terms, but they are all available to the same level to all customers. So they are quite transparent.

Mr NAIRN—What other categories come into the trading terms? I am talking about things like advertising and shelf location. What things do you or your customers potentially use to negotiate variations to those trading terms?

Mr Allara—The trading terms are set. They are available to everybody, as I said earlier. We will obviously try to influence where we are located on the shelf. We do not pay for being on the shelf, but we try to influence where the product is located.

Mr NAIRN—But you do not pay for it?

Mr Allara—We do not pay for it. Research shows that the better the shelf location the better the sales. At the end of the day, where the retailer puts our product is the province of the retailer. We might try to use some techniques to influence that, but that is not our final decision.

Mr NAIRN—Sorry, I am probably using the phrase ‘trading terms’ incorrectly. I am probably using it in a more broader sense. I appreciate that you have a volume and that might determine what base price you will charge. It might also reflect whether you will offer seven, 14, 21, 30 day accounts, et cetera. Beyond that, the evidence from a variety of people is that other negotiations take place in relation to new product lines and advertising. From your company’s point of view, what sorts of areas do you ultimately allow to be involved in negotiations that, at the end of the day, will affect the end price of the product?

Mr Allara—We have promotional programs. Each account will have a series of promotional programs and each account is offered a similar opportunity for that promotional program. They may be at different times of the year or at a different time of the month, but at the end of the day they will all have the same opportunity to have those programs, and that might comprise buying a whole series of things which are used to drive the end consumer sales. If we offer case deals on those things, those same case deals are offered to similar people in the same area. We try to offer people a similar range of opportunities. In the end, it all averages out. With promotions at different times, we try to make sure the whole market gets a similar total percentage discount over a full-year period.

Mr NAIRN—In relation to the timing of some of those promotional things and sharing them across, is that partly based on end performance? How would you make a decision as to how often you offer some of that to Coles as opposed to Woolworths as opposed to AIW as opposed to FAL as opposed to Davids?

Mr Allara—There is a certain frequency to each category. What we do not want to have is, let us say, soup all in one week, because supply chain impact would be enormous. You spread them out to make sure you have sufficient supply while at the same time ensuring people have a chance to have a go at that particular category during a seasonal period.

Mr Toulemonde—But we try to give everyone the same opportunity if there is a promotion.

Mr NAIRN—So there is no discrimination between those who are major customers in that regard?

Mr Allara—No. If we did, we would not have major customers.

Mr NAIRN—What if one of those major customers was gradually getting smaller and smaller and smaller from your point of view? Would that then mean that they have less opportunity for some of those things?

Mr Allara—No.

Senator MURRAY—Mr Allara and Mr Toulemonde, your company is a professional company with very strong brands and a good, strong market share. But I think the real value of you two being here for this committee is probably your international experience. I would assume that both of you have considerable understanding of Unilever's operations internationally and, really, that guides my questioning. You have heard it said, and the committee accepts it as fact, that Australia as a country probably has amongst the highest concentrations of retail power in a few hands as anywhere else in the world, although it has been pointed out to us that in specific market segments that may be replicated in other countries such as in some states of America or in parts of Europe.

My question to you, which is really the committee's question as well, because it is exercising our mind, is that we have to address whether we should limit this concentration of power or let it grow further or in fact reduce it in light of some problems which have been expressed to us. Some problems are cultural and regional diversity and having opportunities for more independence and some are straightforwardly economic. If you get to a critical mass deficiency in the independent sector, the wholesalers cannot survive because they cannot feed off a smaller sector. With that long lead in, my question to you is this: is it your international experience that stronger regulatory regimes in other countries such as the States, which has been mentioned today, in fact enhance the operation of the market from the point of view of manufacturers and contribute to a better economic, social and pricing outcome than has been alleged we enjoy in Australia?

Mr Allara—First of all, I have not worked in the States so I have no direct knowledge of the Robinson-Patman Act in that area. I take one step back and say this: at the end of the day, it is about consumer choice. Consumers choose where they buy or do not buy their products. We have in this country some very successful independent stores. Why is that so?

They are obviously offering consumers the range of products and services they are looking for. Is legislation going to change that? I doubt it.

If you go back 10 or 20 years and compare the range of products that are being sold in the supermarkets today to then, it is quite a staggering change. In those days we had no fresh food, no fruit and vegetables and no prepared meals. There is a major shift in terms of consumer demands. That will not be stopped by legislation. The dry groceries availability is one thing, but the change in consumer offering will not stop. We even heard this week in a report that the amount of money spent outside the home today in Australia is 33 per cent. Ten years ago it was 25 per cent. In the US it is now 50 per cent. We must be mindful of what is happening to the consumer needs.

Senator MURRAY—If the consequence of the way the market is moving were to see the collapse of, say, Davids and FAL because chains, however assigned, had reached a size where that critical mass was gone, would you regard that as a natural consequence of the market, or would you regard that as detrimental to the maintenance of long-term competition? I frame that question against the belief which already underpins our trade practices law—that is, you should maintain competition through diversity. For instance, you are well aware of the merger limitations which exist.

Mr Toulemonde—Maybe I could give a European perspective on this. I left France 15 years ago, so I have to rely on my memory for these types of issues. Concentration in trade is a natural phenomenon. It has been happening in many countries for quite some time. Some countries in Europe are even more concentrated than Australia.

Senator MURRAY—Can you name some?

Mr Toulemonde—Holland is very concentrated. Switzerland is very, very concentrated. Other parts of Europe are less so, but concentration is happening in the retail sector in exactly the same way as it is happening in the manufacturing sector. Looking at the way business is being done here, my impression after having been here for some 2½ years is that the discussion between retailers and manufacturers is very professional. It is done in a very transparent manner. It is done in a very systematic manner and all issues are looked at to reduce costs in the supply chain. The consumer benefits from it.

CHAIR—Do you see some of the regulatory requirements in France as something that we could look at?

Mr Toulemonde—As I said, I left France a long time ago. I am aware that there have been some changes which have not always been to the benefit of smaller retailers, I must say. There has been further concentration following that, but I would not like to comment too much on that.

Senator MURRAY—I appreciate that response, but exercising our mind is the prospect that has been put to us that this critical mass issue could result in Davids and FAL declining to the stage where they cannot carry on as viable businesses doing what they do. By all means diversify, as FAL have, but I want to know as manufacturers, as strong brand marketers, if that would be an issue for you. If you ended up supplying most of your goods to just three or four major retailers and no wholesalers, is that a problem? Is that a concern?

Mr Allara—I think we would prefer a very competitive market. If a competitive market means diversity of offering, then that is a competitive environment, but a competitive market has a broader range of attributes.

Senator BOSWELL—You made a statement before that there are some very successful independent retailers. How are those successful retailers going to survive if there is no-one to distribute to them? We are told that it is 86 per cent in Queensland. It is about 82 per cent around Australia and it is going up, to the point where, if it keeps going that way, the Davids will not be able to survive. How do these successful retailers survive? Who supplies the stores in the country towns with under 5,000 people which Woolworths, Coles and Franklins will not service? This is a concern. With your knowledge, and we are dealing with the real top end of town here with very strong brands which are advertised very heavily by people who protect their brands and their brand names—there are a lot of manufacturers who do not have your advertising clout—how do we keep those successful people out there if we do not have a distribution system that allows them to exist?

Mr Allara—I reiterate that the offering that the consumer now demands is different to what it has been. Groceries are a smaller part of what that full offering was and now is, but they are still a very important part of the offering of a small store. So they must get access to competitive supply of product, otherwise long term they cannot pass on competitive supply to their consumers.

Senator BOSWELL—And there lies the problem.

Mr Allara—It is a dilemma. If we had an answer, we would not be sitting here talking.

Mr NAIRN—In relation to putting a legislative cap on those people, which is what some people are suggesting, how would you view that? How do you think that would affect the marketplace?

Mr Allara—My personal view is that I do not think it would work.

Mr Toulemonde—I share his view.

CHAIR—What about divestment? The NARGA group, the National Association of Retail Grocers of Australia, have said that they would want to see not only a cap but also divestment so we know that one player has more than 25 per cent of the market. How do you see that impacting?

Mr Allara—Again, who is going to take up the balance? Are we going to invite more people to come in who are local players or multinational players? Who wants to come in to take up that shortfall to start with? But you cannot tax success. If people are offering consumers what they are looking for, how do you stop people offering consumers what they are looking for?

Mr NAIRN—Mr Toulemonde, you said you left France 15 years ago. There are various concentrations in Europe. In France, for instance, in some of the more regional areas, are there two or three major players that dominate in that respect? It is different, if you take the whole country. I lived there 20 years ago and I recall that even then there were one or two major players in the supermarket area. Is that happening?

Mr Toulemonde—What happened 20 years ago was the very fast growth of what we call hypermarkets, or very large supermarkets. It was thought necessary to stop the growth of those very large players, so legislation was passed to stop a number of those hypermarkets being built. What happened was that medium-sized supermarkets took over and they basically moved into each medium-sized town, one after the other. So the consequence to the smaller players was the same.

Senator MURRAY—I have a concluding question. I want to take issue with a statement, and I want your response, Mr Allara. I know you said you did not have much detailed international experience in this area but I will give you something that we are all familiar with, and that is the use of the American anti-trust laws, which have been discussed here. One of the most famous cases was the breaking up of Standard Oil of New Jersey into all its constituent parts. The consequence of that was not to cap success but to produce a number of very dynamic petroleum countries. Caltex, for instance, was a California-Texaco mixture, and a series of them has emerged. The latest example of the use of those anti-trust laws or divestiture laws is with Microsoft. Essentially they are saying, ‘Listen, chum. You’re big enough and strong enough. We’re going to clip your wings in some way.’ That has not yet resolved itself, but the use of those laws did not result in the market coming up. It was not a cap on success; it merely allowed different forms of growth.

My question to you is: wouldn’t anti-trust laws or divestiture laws have the same effect? They would simply prevent one or two players dominating the entire market. You might then have four or five players which remain very large—have the economies of scale—and deliver all the consumer choice you are discussing, but you would have a number of large competitors.

One of the other things we have to concern ourselves with is not whether the three retailers become 90 per cent or whatever but that they also might just become two retailers. Based on the question in America, the question for you is: is it axiomatic that the use of the divestiture laws—the use of anti-trust laws and the use of anti-merger laws, which we already have—results in an uncompetitive market and a less efficient market?

Mr Allara—That is a two-way question, Senator. One is that in the States there is a population of 250 million people; we have a population here of 18 million people, growing at less than one per cent. It is a matter of scale and size. Scale could also play a major part now. I am not an economist, so I do not know whether that could transpose itself here, but I think it is an important part of the equation.

Secondly, in some of the questioning this morning I heard about transparency of supply prices. There is an interdependence of retailers and suppliers. Everybody is saying the same thing—that there is transparency. There is clarity of trading terms. It is almost like self-regulation is happening in this area already. It is by default, because nobody wants to get out of bed with one big customer. As one witness this morning said, he would not have a job. We are all in the same boat, so there is a certain amount of interdependence required in this project. Do you get more interdependence by breaking them down into smaller groups of retailers? I do not know.

CHAIR—I have a final question. One of the allegations that is often made is that when Davids had problems some years ago financially, the normal discount markets—the promotional discounts—were simply used by the company for survival reasons. If you start looking back as to where the question of the viability of the small retailers began in earnest, you could date it back to that time. Do you think that is valid, and do you think that Davids continue to absorb the various discounts that you offer because of volume, because of promotional reasons, et cetera?

Mr Allara—I am not privy to Davids' internal workings, but let me say this: if they are passing discounts on, the end market is becoming competitive. We monitor our prices regularly to see that in all sections of the market the price is competitive, or at least within narrow bands. We find it fairly competitive across the whole spectrum.

Senator SCHACHT—Mr Allara and Mr Toulemonde, because you are such big players in the area you operate in and in what you produce, in a sense it is almost an informal vertical integrated system where you are a major player. You have 60 per cent, I think you said, Mr Toulemonde. It can be a very convenient arrangement to have with four or five major retailers if you have 60 per cent. The oligopoly is actually being strengthened because of the dominance of your production of your brand. What opportunity has somebody got to really compete against you in producing toiletries if you already have 60 per cent?

Mr Toulemonde—We have 60 per cent in one particular category. The marketplace is pretty competitive.

CHAIR—Which market is that?

Mr Toulemonde—Deodorants.

Senator SCHACHT—Deodorants are a pretty big part of the market.

Mr Toulemonde—No, it is a small part of the market.

Senator SCHACHT—Okay, you have 60 per cent of the deodorant market. What is the turnover in the deodorant market—$50 million or $200 million a year?

Mr Toulemonde—About $100 million.

Senator SCHACHT—So, 60 per cent of $100 million in my terms—even our Treasurer would agree—is not a bad bit of dough to collect. If someone else is going to come into the marketplace for deodorants, you have a system of distribution, very efficient production, and so on. You have a good relationship with the five majors. The person starting off—coming in to compete—might not even try when they see that you have 60 per cent of the market and a good relationship on the retail side. You will always be the dominating influence, and therefore the oligopoly continues.

Mr Toulemonde—That is not the case. We actually have quite a bit of competition, even in that category, and we cannot prevent anyone entering the market.

Senator SCHACHT—If you were drawing up a business plan and someone had 60 per cent, you might take a deep breath before you approached your bankers and financiers to say, 'We're going to take on somebody who has 60 per cent of the market.'

Mr Toulemonde—That is a decision any manufacturer has to make. I can say it applies to some categories for us as well.

Mr NAIRN—Surely the rule is that people can enter the market—

Senator SCHACHT—They can enter the market formally, yes. The reality is that if someone has 60 per cent of a particular market, a good distribution system and a good relationship with the retailers in the supermarkets, you might think twice about taking that on.

Senator BOSWELL—What Senator Schacht is saying is quite correct. He is saying is that you are preventing innovation because someone like me who wanted to make deodorant has not got anywhere to sell to because there are only about three or four people you can sell to in this country. They are very happy with you, you have a great product and you advertise it well, and it is a good brand name so, because there is nowhere else in the market for someone who wants to create another brand, there is no room in the market unless you have other retailers out there.

Mr Allara—All the major chains encourage diversity of offerings because that gets consumers in. Whether you are Unilever, Bill Bloggs, Gillette or anybody else, they will look at an offering that is adding value for a consumer. Just look at the diversity on the shelves that there is today. Just look at the tea section—the diversity of supply in the tea section today is enormous. There are small manufacturers, small importers and majors. It is there because the thing called competition helps that process.

Senator SCHACHT—How much has Unilever got of the tea market?

Mr Allara—Around 40 per cent.

Senator MURRAY—That is contrary to the evidence we have received. Country stores tell us that, when the store goes from independent local hands into national hands in that same country town, the local suppliers lose out. The supply chain becomes national and metropolitan there, and local suppliers lose out. That is the question that faces you: how do you get your beans and your small products onto the shelves? So I am not certain that your answer is correct in terms of experience in some of the markets.

Mr Allara—It depends on what category you are interested in. Not too many people are going to set up a detergent tower to go into a small country town to supply a local market, so it depends what category you are in and what the asset investment is as well. But if you are going to sell a prepared meal, they can quite easily do that.

CHAIR—I tend to agree with you, Mr Allara. If somebody has an innovative product that is price competitive, certainly the majors would not say no, as I would expect, but we could not expect you to say otherwise as well. Thank you for throwing in this final question, Senator Schacht. Thank you for coming, I appreciate it. We regret that our former colleague has not been able to be grilled, but so be it.

Evidence was then taken in camera, but later resumed in public—

[1.36 p.m.]

CAHILL, Mr Richard Peter, Research Analyst—Retail Sector, ABN AMRO

METH, Mr Glynn David, Associate Director (Store Analyst and Portfolio Manager), Rothschild Australia Asset Management

CHAIR—Welcome. The committee prefers all evidence to be given in public. However, you may at any time wish to go into in camera, and the committee will take that request on board. I remind you that giving of false or misleading evidence may constitute a contempt of parliament. The committee has before it confidential submission No. 331 from Mr Meth. Are there any alterations or additions you wish to make at this stage?

Mr Meth—No.

CHAIR—Before I invite you to make an opening statement, could I clarify that neither of you gentlemen has any conflicting areas of interest in terms of working for either of the three majors—Coles, Woolworths, Franklins? Or Davids?

Mr Cahill—Not to my knowledge, no.

Mr Meth—In terms of conflicting interest, we at times have had and might have shares in any of the three majors and Davids—basically as part of the funds under management—and also in the minor stocks as well.

CHAIR—It is better to put it on the record first so that we know, because there was an attempt to choose someone as independent as possible.

Mr Cahill—To the best of my knowledge, I am not an employee of—nor receiving any fees from—major retailers, but it is entirely possible that our corporate department could, without my knowledge, be in discussions with the major retailers. I am not aware of that.

CHAIR—And I need to state on the record that I used to be on the board of ABN AMRO—if it comes back at any time. It was chosen because of its independence. Having said that, I invite you to open the batting.

Mr Cahill—I would like to make some general starting comments about the question of market cap impact on the market or indeed on the market capitalisation of the listed retailers. As with any business, the profitability of the grocery retailers is a function of the volumes they are selling, and they are sensitive to the level of those volumes. Clearly, any reduction in the volumes sold by Woolworths or Coles, for example, would put some downward pressure on their margins and would tend to be a negative impact on their profitability. The opposite clearly would apply to any of the retailers who picked up market share or volume, so it is stating the obvious but it is worth while stating anyway.

The other issue in terms of the impact that that would have on the market capitalisation or the share price for the listed retailers is that there would have to be some greater uncertainty applied by potential investors to the price and the rating they would give to the major listed retail stocks if there were market share caps and there were enforced shedding of market share volume for the major retailers. It is virtually impossible to know how severe that would be, but it is an issue.

Mr Meth—I will give a summary of a couple of the points we raised. We looked at it from the point of view of the financial implications of the cap on the major retailers. It came down to essentially two areas we looked at: the cash flow and the risk and uncertainty which would apply to them. Although the direction appeared clear in terms of how it would impact, the dollar value and the duration were two things which were essentially non-quantifiable which we could come up with. In terms of the majors, we would see the operating cash flow obviously negative for the Coles Myer and Woolworths if there was a cap placed and if they had to sell down to the 25 per cent max. Also it would be potentially positive for Franklins, because they would essentially have a free run.

The other thing is that there would be increased risk, and that would obviously imply increase cost of capital. That would apply to the retailers as a whole—and how long that extended for in the market we would not be able to come up with.

A couple of key points which we thought came out were that if there was a forced divestiture the price of outlets would obviously decrease over that period of five years. That would have a positive impact for Dairy Farmers International—they would be able to pick up the outlets at reduced prices. But then there would be a negative impact for essentially the other two majors—and also for the independent property owners who own the sites on which they are situated and also any independents over that period of time who were actually wanting to sell out their retail operations. Their superannuation funds would be impacted by that. Those are a couple of key areas. I am sure you can raise the rest in the questions.

Senator BOSWELL—Can you tell us how many Woolworths and Coles shareholders there would be?

Mr Cahill—It would be of the magnitude of a couple of hundred thousand to 300,000 for both.

Mr Meth—In terms of Coles Myer I believe it is about 300,000 to 400,000.

Mr NAIRN—Woolworths is 340,000.

Senator BOSWELL—Are they independent shareholders? What are Coles shares at the moment?

Mr Cahill—Coles Myer shares are worth just over $9.

Senator BOSWELL—And what are Woolworths shares?

Mr Meth—Five dollars.

Mr Cahill—About $5.45 or $5.50.

Senator BOSWELL—To get to that cap, Coles would have to drop about 30 per cent of their sales, wouldn't they—or is it Woolworths?

Mr Meth—Woolworths.

Senator BOSWELL—What would the impact be of taking 30 per cent off a retail business? It would drop the shares, but by how much?

Mr Cahill—It is impossible to say, because it is a function of the impact it is going to have on their profitability, and that is going to be a function of how they can adapt their cost structure to the different volumes.

Mr FITZGIBBON—They would still be a good buy.

Senator SCHACHT—The price will drop if this gets out to the Stock Exchange this afternoon.

Mr NAIRN—This has been discussed numerous times.

Mr Meth—Apart from that, it will also have an impact on the risk factor applied to the shares, so apart from the cash flow that risk factor would also knock the share price—and that would not just be for the retailers but for the market as a whole as offshore investors saw the intervention that was taking place in the local market.

Senator BOSWELL—So what would the offshore investors do?

Mr Meth—They would push up the risk factor applied to Australia. Again, there is the duration—you do not know how long this is going to last.

Senator BOSWELL—Or how long the cap will last?

Mr Meth—For how long the offshore investors are going to perceive that there is an increased risk in holding investments in Australia. You do not know the extent to which it is going to be and how long it is going to be.

Senator BOSWELL—So it might push the shares of everything in Australia up?

Mr Meth—No, it will push them down.

Senator BOSWELL—So it would drop the shares of everything?

Mr Meth—Yes.

Senator BOSWELL—Not just Woolworths and Coles?

Mr Meth—It would have a broader impact than just on the retail sector.

Senator SCHACHT—They can always shuffle shares in Indonesia, Thailand, Burma, China and all those other well known places that are secure for investors! I know there is an impact in all of this but Australia has a stable economic and political climate irrespective of which government is in power. That does count for a heck of a lot. In America, when the Sherman trust act came in during the 1900s, what happened to American investors? Did the share market collapse? Did people from Europe stop investing in America?

CHAIR—I think we are asking, however, about a different aspect. You are asking a theoretical question.

Senator SCHACHT—But we have had the theoretical position that there is going to be an overall impact on the stock exchange in which two companies will be significantly depressed and that there is going to be a broader impact on investor attitude towards Australia.

Mr Meth—The point which I made was that, first of all, it was non-quantifiable. That was the first issue and the second thing was the duration: you could not put a time limit on how long it would be. It might last a day. It might last a week. It might last longer.

CHAIR—In terms of the market generally?

Mr Meth—Yes.

Mr NAIRN—Either of you might not be qualified to comment, but what do you think such a move would do to competition in the retail sector generally?

Mr Cahill—It is very hard to tell. Say, for example, you decide to have a maximum of 25 per cent of the market being held by one of the participants and you apply that on a state by state basis. In the major Australian states there tend to be only four competitors in grocery retail and wholesale, so you would always end up with a situation where it is going to be the existing four competitors with 25 per cent, each totally unable to actually increase or decrease their market share. You would achieve a situation which would be unworkable. That is just an impression about the difficulties of trying to implement that cap plus the 25 per cent maximum.

Mr NAIRN—It would be unlikely to improve competition across that industry.

Mr Cahill—It does not seem to me that it would in those circumstances.

Mr Meth—In the submission we gave you there is a point which relates to it as basically being like this: if you have, further down the track, three players at the 25 per cent level and each of the players is trying to increase their returns to their shareholders, we believe there would be an incentive for there to be actually less competition, basically pushing up the prices.

Mr NAIRN—It would almost be an incentive for collusion.

Mr Meth—Almost, yes.

Senator SCHACHT—Are you saying the Trade Practices Commission would not be effective in stopping such collusion?

Mr Meth—That is a different question. There would be an incentive for collusion rather than whether that would actually be achieved or not.

Senator SCHACHT—Perhaps an incentive for $10 million fines too. Maybe you should recommend to us that we should put jail sentences in as well; that would sort a few people out.

CHAIR—What about the vulnerability of these companies to foreign takeover? How would you see it if divestment requirements were announced? Would that be feasible? Would there be a slump in price? How do you see the scenario playing out?

Mr Meth—The scenario which you had was a five-year sell-down period. If you were in the position of a retailer being forced to sell down, you would have a number of actions to take. You would sell off your worst performing stores.

CHAIR—Where would they be?

Mr Meth—They would be anywhere but essentially they would be your worst performing stores. If you had two stores close to each other, there was a third competitor nearby and you were not achieving an adequate return, those would be the ones that you would sell off; those are the ones that you try to identify to dispose of. Then again, it comes down to your definition of your 75 per cent and your 25 per cent per chain—whether it is geographically over Australia, per state or in the local area—as to what they would actually be forced to sell off. So that would be the first inhibitor to an outsider being able to make a large acquisition.

The other thing is that, if you are doing it over a five-year period and you are trickling out, it will be difficult for a person to build up an immediate critical mass so as to be able to move. So I would say, no, that would not be a catalyst for an outsider to come and take a new share. Where it might be a catalyst might be that, if it had an impact on the market capitalisation of Woolworths and Coles Myer, an outsider could possibly see it as an opportunity to take out one of those two chains.

Mr Cahill—With the catch that potentially they are going to look at maybe Coles or Woolworths and say, ‘I’m buying a company that can only go to a 25 per cent market share.’ Globally, that is an uncommon restriction so it might be seen as making the company less attractive.

Senator SCHACHT—You are saying this is a restriction because they are stuck at 25 per cent? Tell me a country in the western world that already has a supermarket chain that has 25 per cent of the market?

Mr Cahill—You are right. I did not say it was common to one and common to another. I was just making the comment that in today's terms in Australia you can buy—if you wanted to—one of the major retailers without a restriction on being able to grow the market share of that retailer. I was just making the comment that if you actually put a cap on the retailer that would make it a less attractive takeover target in that there is no growth potential in that retailer anymore.

Senator SCHACHT—But this does not take account of the fact that the government has available to it regulation through the FIRB to stop a foreign takeover anyway if it is not seen as being in the national interest.

Mr Cahill—That is another question.

Senator SCHACHT—But it is in the formula.

Senator MURRAY—Can I explore this point. We already have market caps in our law. We already have it established that companies cannot grow beyond a certain size, because that is exactly what the ACCC does. Every time a major merger is offered which will lessen competition, the ACCC turns it down, and it has done so this year, has done so in the past and will continue to do so in the future with very little detrimental effect, in fact with a positive effect. I would like your response to that because all that has been proposed is a version of that which deals with incremental acquisition or chequebook purchases. So it is not merger driven; it is incremental growth.

The second thing is that there are numerous instances worldwide where divestment has in fact increased the core value of the particular companies. That is frequently done when one company buys another. They sell off all sorts of bits to ensure that the core business of the company actually grows and there is nothing to prevent the money so released in Coles, Woolworths or some other group from being used as freed up capital to enable them to grow their company externally to move into other areas of business. It is not as if you cannot be a core supermarket operator in Australia and be just as capable a core supermarket operator elsewhere. Daewoo, for instance, has done it in the reverse way, coming into Australia; it being the Japanese retail agent. So I just want to query the assumption that there are automatic negatives and that it is contrary to existing Australian practice, because it is not.

Senator BOSWELL—Wouldn't the independents buy up the stores they have to divest?

Mr Cahill—Inevitably, they would be one of the groups who could buy them. The other one in Australia's current market situation is Franklins. Yes, if they have to be sold, they are the only buyers, so I agree that that is logical. Mr Meth mentioned earlier the situation whereby an independent retailer at the moment who may be wishing to sell his store to one of the major retailers would be unable to do that if we had the proposed market share cap. So it cuts both ways. But I agree with you.

Senator MURRAY—Could you respond to my question, please.

Mr Meth—There are a number of issues in your question. There are a couple which I would like to address. First, in putting the cap on, you are not saying that they cannot grow further. You are basically putting the cap on to Woolworths and Coles and saying that they must divest.

Senator MURRAY—In that field?

Mr Meth—Yes, in that particular field.

Senator MURRAY—But not, say, in shoes or toys or whatever.

Mr Meth—Yes. Many of the divestitures which we have actually seen have been divestitures of different business units so that the company is actually coming down to a core competency which might be retail. Essentially, what you are saying there is, 'Sell-off part of your core competency.'

Senator MURRAY—If I may interrupt with an example, I think that what happened in Great Britain in the 1980s was that the major brewing chains were required to reduce their vertically integrated holdings of hotels—on-consumption outlets, in particular, as well as off-consumption outlets. The consequence was a value improvement. In one case, a major new business was formed—the Grand Metropolitan Hotel and off-consumption chain.

Mr Meth—Again, I think you are talking of two businesses, aren't you? You are talking about one which is a hotel business and another which is a brewing business, and they divested the hotel from the brewing.

Senator MURRAY—But if you look at Coles Myer, it has got numerous businesses in there. It has numerous retail businesses in different retail categories. It has the department store business. It has a number of distinct businesses and, although its core business is retailing, in that sense it is a diversified group. If you look at Woolworths, it has a wholesale group as well as a retail group.

Mr Meth—Yes, but in the question basically Coles Myer in the supermarket side of the business would be divesting off down to a 25 per cent market share. That means that Coles Myer would be divesting part of a core business. If it divested its entire supermarket business, whoever the buyer was in Australia would still have to divest some supermarkets.

Senator MURRAY—But the analogy I am drawing with you in the Great Britain instance is that, if you take the hotel's off-consumption business, it would have reduced with say Courage or one of those big groups—I am just making up figures because I do not know the actual figures—from maybe 500 outlets down to 300. What is different? If it works in a major sophisticated modern Western economy for other countries, what is different here? Why would it collapse value and collapse investor confidence in the market? We have an international precedent. That is the point I am making.

Mr Meth—In terms of there being a negative impact on the markets, the risk factors which would come in would be concerns regarding what the basket was that the 25 per cent is going to be calculated at. Is that going to be a permanent basket going forward into the future? How can we actually ensure that we remain at this 25 per cent level this year and next year if more items are brought in? A question for the supermarkets would be: should they start focusing less on that basket and focusing more on other industries? That would then create pressure to bring other particular products into the basket. Does the basket then change and your 25 per cent calculation change?

Once you have started that 25 per cent rule, there will be potential for that to change further down the track. How does it apply geographically? Do you actually have a solution if the supermarkets have to sell down to 25 per cent yet they maintain a concentrated area in a locality and Woolworths or Coles Myer dominates a local area? Have you achieved your objective? If you have not, that creates further uncertainty in the market that you might do something again further down the track.

Senator MURRAY—Surely those questions apply to any country—and, indeed, already apply in Australia—seeking to limit growth in the interests of competition. So, when you prevent a merger of one company with another, those considerations may apply. In foreign jurisdictions, when there is forced divestitures or a forced maintenance of a cap, those considerations apply. The questions you ask are important, meaningful and proper questions, but the fact is that they can be resolved. What I really wanted to ask was not that but: would it be detrimental to the market overall? As I understand it, that lies behind your presentation. You are saying that it will be detrimental for the economy and for the companies themselves.

Mr Meth—I said the market impact would be negative for the companies involved.

Senator MURRAY—But you also said it would be negative in terms of international investor—

Mr Meth—The perceptions that international investors would have of the Australian market would also be negative.

Mr Cahill—Is that just because of the uncertainty created?

Mr Meth—That would be because of the uncertainty created by this. It would also be because of the—

Senator MURRAY—Why is it any less certain than an investor looking at Microsoft, for instance, who might be wary that at some stage they are going to reach a size where the antitrust law is going to come in? Why is it so much different for us when those laws already apply elsewhere?

Mr Cahill—The size of the market surely plays some part in that.

Senator MURRAY—We have a very diverse market. Twenty-five per cent in the supermarket area is not going to affect our minerals and industrial index.

Mr Meth—I believe that it probably did impact on the Microsoft numbers. We obviously do not know. It is not an area that I am familiar with, but when that case was going on I would imagine that investors took that into account when they made the investments. Investors coming to Australia and investing in Australia would take it into account in determining whether they should be investing here and what they should be paying for the assets.

Senator MURRAY—In that industry sector.

Mr Meth—But it has a broader impact. If they see that regulation has been applied to one sector, are they in other sectors where similar legislation might apply?

Senator SCHACHT—Can I just point out that in the media—not on the product side but on the shareholding side—you cannot own more than 25 per cent of a television station in Australia, and you cannot own more than 15 per cent of both a television network and a newspaper chain. Those rules are there. I notice that neither Packer, Murdoch nor Fairfax seem to be falling over—they seem to be doing quite well. No-one has ever written it up that this has had a detrimental effect on the rest of the stock market.

Senator BOSWELL—But they were not allowed to acquire any more—they did not have to divest any more.

Senator SCHACHT—Effectively, it got the Herald and Weekly Times out of owning Channel 7. It got more players and you end up with a healthier market and, in the end, you have a healthier economy because there are more players.

CHAIR—Could we return to our experts.

Senator SCHACHT—I'm just a mug amateur—I know that—but—

CHAIR—No, there was no implication in terms of the senator.

Mr Meth—The other point we made was that the extent and duration could not be determined. I think the key element there is the duration. You were talking about the media. It could reverse in a matter of days if a major positive announcement were made about Australia. The whole impact would be reversed virtually immediately.

CHAIR—I think that is about it.

Senator SCHACHT—I have one other question.

CHAIR—Before you ask it, I have one. Do you know where the concentration of Woolworths and Coles Myer shareholders is? Are they predominantly Australian?

Mr Meth—In Coles Myer it is definitely predominantly Australian. Because of the incentive system which they operate, you will see that there are an enormous number of shareholders who have around 500 shares each—

Senator MURRAY—It is a very clever scheme.

CHAIR—They give them a discount.

Mr Meth—who receive a discount card. Because of that, you have a very large Australian based shareholding. It tends to be small shareholders.

CHAIR—Is Woolworths the same?

Mr Meth—Woolworths do not have the same system. I am not sure of their register at all.

CHAIR—In terms of this divestment capping, have you given any thought to what might be the implications for employment?

Mr Meth—I would not have any expectations.

Senator SCHACHT—I have two questions. Talking about the impact on shares, has the ongoing imbroglio about the Yannon case had any detrimental effect on the share price of Coles Myer?

Mr Meth—At the particular point in time, I believe it did have an impact.

Senator SCHACHT—But it is not having an impact now?

Mr Meth—That is the point of duration which I mentioned earlier.

Senator SCHACHT—I raised this other question with Woolworths before us. The argument about not having a cap is to let growing companies in Australia be able to compete with international companies that may try to move into Australia—those dreaded foreigners. I can understand part of that argument. But if they are going to be given this advantage, they will become very dominant players in the Australian market. With all of their skill in Australia, do you have a view about them helping Australia's national interest—our current account and international trade performance—by becoming major players in the Asia-Pacific region by developing supermarkets?

Mr Cahill—That is really a matter of policy for the company. I would not want to get into that.

Senator SCHACHT—But if the company made that announcement, what would it do to the share price?

Mr Cahill—Again, it is quite hard to tell. It would depend on where they were buying, whether they bought a small or a large business and whether it were something they were regarded as being able to add value to. It may be a positive, but you cannot be sure.

Mr Meth—Some Australian companies overseas have been extremely successful, and some less so.

Senator SCHACHT—In the retail sector?

Mr Meth—Not in retail—in other areas.

Senator BOSWELL—The beginning of this was when Davids crashed overseas, and that started the rotting. They went overseas and went belly up.

Senator SCHACHT—They are using the argument that you need a bigger size in Australia, that you cannot be capped and that you need to have the defence of the Australian market. That is an argument which a number of other Australian companies in other sectors have used against restriction. Mr Packer used it at one stage to say, 'I want to be able to compete overseas. You cannot cap me in Australia,' whatever the form of the legislation was. If they are going to seek the benefit of being able to have such a dominant part of the market, what benefit would they give back to Australia? One area would be using their skill to get into exporting services, running supermarkets in Asia and making that the basis of having Australian products sold in Australian owned supermarkets overseas.

CHAIR—Thank you, Mr Meth and Mr Cahill. We appreciate having you here as our expert witnesses. We may come back to you when writing our report to see whether there is anything new. We appreciate your time and apologise for the delay you experienced. Is there anything you would like to say finally?

Mr Cahill—No, that is it. Thanks very much.

Committee adjourned at 2.08 p.m.