

ACCC Grocery Inquiry

Coles Supermarkets' Response to ACCC Interim Report

1 Overview

Coles welcomes the opportunity to respond to the ACCC's Interim Report in the inquiry into markets for the supply of groceries (*Inquiry*).

Coles acknowledges the significant contribution of a broad range of stakeholders to the Inquiry to date and has listened to the feedback raised by all stakeholders.

Consumer groups and fresh produce suppliers in particular have raised concerns about aspects of supermarket operations that they believe could be improved, including greater transparency and additional information to assist them in their decision making when buying from or supplying to supermarkets. Coles is committed to continuous improvement of its own business and the sector more generally and it welcomes further engagement and involvement in proposed solutions to the matters raised.

This submission sets out Coles' response to the ACCC's Interim Report. It is structured around four broad topic areas – customer experience (see section 3), suppliers (see section 4), retail competition (see section 5) and supermarket profitability (see section 6). Coles has made eight recommendations for the ACCC to consider (as set out in the body of the submission and outlined in Appendix A) which it believes would help to:

- Empower consumers by giving them greater ability to switch and search with ease;
- Increase dynamic rivalry in the market while ensuring it continues to be increasingly competitive; and
- Balance transparency and fairness for suppliers with enduring value for consumers.

2 Executive Summary

2.1 Customer experience

(a) Shrinkflation

Coles' experience is that suppliers typically reduce the weight or pack size of a product where they are facing rising production costs and consider that a pack size or weight change is preferable to a cost price increase which is likely to result in an increase to the retail price for consumers.

Coles has greater control of pack sizes of Coles Brand products. We aim to keep the size of our products stable, but just like some of our suppliers, we have in the past 12 months decreased some Coles Brand pack sizes. In the last 12 months, just 0.5% of our Coles Brand products have had a decrease in pack size.

Coles understands and acknowledges customers' concerns with changes in weight or pack size, particularly for critical household items in the current economic climate. Coles is open to exploring measures to enhance customer transparency in this area as part of an industry wide solution, noting that any impacts to suppliers and Grocery Code compliance will need to be carefully considered.

(b) Clarity around promotional rules

As noted in Coles' submission to the Issues Paper, grocery retailers currently formulate their own internal compliance guardrails regarding how often products can be promoted and how long the higher shelf price must be established before the price can drop and a discount be claimed. Coles previously submitted that both competition and consumer outcomes in grocery could be enhanced by the ACCC publishing more detailed guidance on pricing and promotional claims. Compliance guardrails of this kind must necessarily strike a balance between facilitating and restricting

competitive pricing – the longer that the regular shelf price is established, the lower the risk that a discount claim will be regarded as non-genuine and therefore misleading, but equally, the less often the product will be discounted, therefore reducing price competition in the market and savings for customers.

As the ACCC has recently commenced litigation against Coles and Woolworths regarding one promotional type, it may be necessary for court outcomes to be considered as part of the development of additional ACCC guidance for the industry.

(c) Transparency of prices

Coles believes that specials and promotions continue to offer strong value to customers and assist them to reduce the cost of their shopping. However, Coles notes the feedback from consumer groups and customers regarding improving clarity and understanding of promotions.

Coles is currently updating its website to make it easier for customers to identify value across Coles' stores and understand the different promotional types. Coles is also looking at ways to better inform customers when there are major supply changes that will impact retail pricing such as severe weather (e.g., which may damage fruit and lead to shortages of supply) or bio-security issues (e.g., which may result in restrictions on transporting produce across state borders and lead to shortages of supply).

Coles observes that consumers are comparing prices before shopping more than ever before. There is evidence that when consumers search more, it can substantially improve the competitive dynamics in a market. This underscores the importance of ensuring that it is easy for consumers to do so. Coles publishes its pricing information online and it is available to be 'scraped' by price comparison websites and apps. If other retailers provided their information in a similar manner, this would enable customers and third-party comparison websites to more readily provide information to customers that would enable them to make comparisons between different retailers.

Coles considers that CHOICE's mystery grocery basket shop could play a more meaningful role in educating customers about price competition if the actual brands purchased as part of the mystery shop were disclosed to consumers. Because ALDI primarily sells private label products, it is unclear at present whether CHOICE is comparing 'like for like' in the products selected. Publishing the products actually purchased would enable customers to review the results of the mystery shop themselves and assess both the quality and the price of the basket shopped.

(d) Unit pricing

Unit pricing assists customers to compare prices both in-store and between supermarkets and Coles takes compliance in this area seriously. Coles is open to exploring options for improvements (noting the Federal Government's recent announcement of a review of the Grocery Code), such as requiring greater consistency with units of measure. Coles is also open to reforms regarding improved readability, although it will be important that any new requirements can be operationalised in practice, including with respect to electronic labels. Coles sees merit in the requirements being extended to other grocery retailers (potentially subject to a minimum size requirement) to further assist customers.

(e) Regional pricing

One potential concern raised in the Interim Report is whether customers in regional areas pay higher prices for groceries than in metropolitan areas. Since 2010, Coles has had uniform statewide pricing in place which means that regional and metropolitan customers receive the same pricing offers regardless of location and the number of competitors in their local area. In practice, the vast majority of products are priced the same nationally. The only exception to Coles' statewide pricing policy is in relation to 13 stores located in more remote areas that apply an additional freight component into their retail pricing. These are 8 stores in the Northern Territory and 5 stores in WA. Notwithstanding this, some key value items such as meat categories do not have the additional freight component applied and are priced the same across WA. Coles absorbs the higher costs of freighting these staples to very remote stores.

The state and nationwide pricing policies of the largest supermarket chains are facilitated by their scale and are a significant benefit to Australian consumers living in regional areas.

(f) Multi-buys

Another area of concern raised in the Interim Report is whether multi-buy offers support optimal consumer decision making and should be permitted, particularly on essential items. Multi-buys (where consumers receive a discount for

purchasing two or more products) are one promotional type offered by Coles in conjunction with the suppliers of those products.

Coles does not support policy measures which would in effect restrict price competition between retailers. Coles considers that multi-buys offer strong value to customers who are prepared to purchase in larger quantities in order to access lower prices, and they are one way that Coles competes with Costco, Bunnings and other grocery retailers who sell bulk offers. For customers who only wish to purchase a single unit, Coles offers many other discounts. Multi-buys can also be desirable to suppliers as a means of supplying additional volumes, including in order to help clear inventory given shelf-life limits. We would advise against restricting multi-buys offers, but agree that unit pricing should be clearly displayed.

2.2 Suppliers

(a) Fresh produce volumes and pricing

As Coles identified in its response to the Issues Paper, the procurement of fresh produce is more complex than in other perishable supply chains such as meat and dairy. This is because (a) the supplier base is highly fragmented, (b) production can be affected by variable weather conditions, and (c) consumer purchasing patterns can change quickly (e.g., customers may trade from one product into another in response to price changes, for example switching from one fruit to a different type which has dropped in price due to abundant supply). All of these factors combine to make it more difficult to predict volume requirements and market prices for fresh produce.

Coles acknowledges the concerns raised by growers in this area which Coles believes are exacerbated by information asymmetries and a lack of transparency at various points in the supply chain, particularly when growers sell via aggregators rather than direct to supermarkets.

Coles is examining ways in which it can improve the current ordering and volume commitment process to reduce situations in which there are significant changes in volumes than those agreed prior to the growing season. Coles also welcomes a discussion on other areas for improvement, including potentially through centralised publication of pricing and volume data.

Coles notes Treasury's current consideration of Grocery Code revisions following the Emerson Review, and strongly submits that any amendments to the Code must not impose obstacles to efficient and fair contracting with suppliers, or create disincentives to deal with particular suppliers. For example, the proposed deeming of ordinary commercial activities like reducing the volumes ordered from a supplier to constitute an act of retribution against that supplier is likely to act as a disincentive for supermarkets to contract directly with smaller growers. We believe that a well-defined Code should strike the right balance between the fair treatment of suppliers and ensuring best value for consumers now and into the future.

(b) Quality assurance

One concern raised by stakeholders is whether quality assessment and rejection processes are being used for purposes other than genuine quality issues, including to manage the volumes supermarkets receive.

Coles acknowledges that it can be particularly difficult for suppliers when fresh produce is rejected, especially where the quality issues are due to weather events beyond the control of the supplier. However, Coles has found no evidence of produce being rejected for reasons other than genuine quality issues.

Coles has a responsibility to its customers to conduct rigorous quality assurance over fresh produce to ensure produce sold in its stores meets consumer expectations. The quality team, who conduct those assessments, is independent of the fresh produce buying team and has no role in formulating forecasts or placing orders with suppliers. A quality inspection involves assessing the produce against each of the criteria listed in the relevant specifications, with the results documented in each case and sent to the supplier in the event that produce fails the quality inspection. Further, Coles' Distribution Centre (DC) quality program is independently audited and reviewed by a third party. The volume of fresh produce rejected by Coles is low. In FY23, Coles rejected just 1.49% of the fresh produce cartons it received from suppliers. Coles would be open to recommendations by the ACCC that might enable suppliers to be assured of the independence of this process.

Coles again notes that proposed amendments to the Grocery Code that would reverse the onus of proof such that the rejection of fresh produce that did not meet specifications would be assumed to be an act of retribution against a supplier are unwarranted and are again likely to act as a disincentive to contract with smaller suppliers.

(c) Cost price increases

One concern that has been raised by some suppliers of packaged product is whether they have an effective ability to negotiate cost price increases with the major supermarket chains.

For every \$100 of operating revenue of Coles Group in FY23, the cost to purchase and transport products to stores was \$73. These costs are a major driver of the retail price. To keep retail prices low, it is therefore important for supermarkets to both negotiate competitive cost prices and validate cost price increase requests to ensure that they are appropriate.

Coles assesses all cost price increase requests in accordance with its cost price adjustment policy and it has not been Coles' experience that suppliers cannot successfully negotiate cost price increases. In analysis Coles has conducted for cost price increase requests in the last 5 years, Coles has accepted over 90% of the value of the cost price increase requests received from suppliers, including \$3.88 billion in price increases from packaged suppliers since FY22.

(d) Rebates

Some suppliers have queried the value and transparency of rebates such as volume rebates and settlement discounts and the ACCC has foreshadowed that it will consider this issue further in its final report.

There are a number of supplier terms and rebates in place. Trading terms such as volume rebates and settlement discounts are largely a historical feature of the grocery industry which enabled suppliers to have a consistent wholesale or list price with all of their customers but then provide larger customers a rebate for benefits such as lower counterparty risk, better payment terms and security, easier administrative processes and the inherently larger volumes supplied. Trading terms are negotiated at the outset of the trading relationships, recorded in writing in accordance with the Grocery Code and are clearly specified on claims / remittance documents.

(e) Promotions

Promotions on supermarket products provide important benefits to retailers, suppliers and customers. For suppliers, this includes substantially increased volumes, promotion of their brand and an opportunity to engage new customers who have the potential to become long term repeat customers. Because of the benefits to suppliers, funding of promotions is commonly shared between Coles and its suppliers. In FY24, Coles contributed the majority of funding to the cost of price reductions on packaged product. The proportion funded by Coles has increased since 2019. Where products appear in the Coles catalogue or on a Promotional End, this is funded by Coles in the majority of cases. Coles seeks to use these placements to highlight products that represent great value for customers and which it expects to sell at high volume.

2.3 Retail competition

(a) Price together with other aspects of competition must be considered

Price is a very important aspect of retail competition and it is appropriate that price competition is examined in detail as part of the Inquiry, particularly during the current economic climate. However, value represents more than price to the customer and other aspects of competition and drivers of customers' choice such as quality, range, service, consistent availability, convenience, location and immediacy are also important and receive only limited consideration in the Interim Report. Coles supports a comprehensive review of these other aspects of competition.

Coles' own experience pre-demerger in 2018 was that a focus on price competition for a number of years over and above other drivers of value had reduced Coles' competitive position. Reduced investment in Coles' fresh food offering and store expansion and renewal program together with range reductions alienated many customers, resulting in declines in Coles' market share. Since demerger, Coles' corporate strategy has been to focus on price competition but also on other drivers of value. Coles' subsequent investments in store refurbishment, store format, own brand product development, range (especially in health, convenience), and immediacy and home delivery reflect very vigorous competition in areas additional to price.

(b) Cost management and efficient capex investment

A critical factor in competition in the supermarket industry is the ability to minimise the need to pass on increases in operating costs, such as increasing occupancy and logistics costs and wage rates, through efficiency programs and capex investments. In addition to offsetting cost increases, these programs create savings that are reinvested into other revenue generating activity, like additional promotional activity.

In terms of efficiency programs, since 2019 Coles has had two major cost out programs: Smarter Selling, and Simply to Save and Invest. Collectively they have delivered to date savings of over \$1.2 billion. These programs have seen savings through key initiatives such as in-store energy saving programs for HVAC and refrigeration, re-alignment of the meat operating model, improved mark down processes for fresh produce and dairy and loss initiatives.

In terms of capex investments that aim to reduce operating costs, there is significant competitive pressure for major supermarket operators to maintain a sophisticated capex program that continually modernises the assets used to store and distribute products to customers, from new automated warehousing systems, improved primary and secondary transportation and backhaul scheduling systems, in-store features like self-check outs, to home delivery options like Click & Collect. The infrastructure required to operate a nation-wide grocery supply operation in a country with the geographic scale of Australia is one of the reasons that Australian supermarkets have a capex-to-sales ratio that is substantially higher than large overseas supermarket operators.

This feature of competition in the industry has seen Coles invest approximately \$1.5 billion in modernising its distribution systems both at the warehouse and customer delivery level through Automated DCs and Customer Fulfilment Centres. Coles has a globally leading platform, which is the result of the intense competitive pressure to offset operating costs. This feature of competition is essential and is not addressed by the Interim Report.

We contend that these substantial efforts to reduce cost are further evidence of strong competition incentives in the market. Competition, when it works well, is not just about lower prices and improved quality, range and service, but also about cost reduction, greater efficiency and innovation over time.

(c) Barriers to entry

The Interim Report does not express a view on the level of competition in grocery retailing but it suggests that Australia's supermarkets sector is highly concentrated.¹

When regard is had to Australia's geography and relative population size, Coles does not consider the current number of national supermarket chains (Coles, Woolworths, ALDI and IGA) to be surprising. It takes time and cost to build a national network, and Coles' and Woolworths' own networks have taken many years to establish. However, ALDI's rapid growth in Australia demonstrates that new supermarket chains can enter and expand over time and Coles considers that the Australian grocery sector remains an attractive market for overseas grocery chains as well as expansion by local players.

While building a store network takes time, Coles does not consider access to sites to be an insurmountable barrier to entry or expansion. Given their similar store formats, Coles most commonly competes head-to-head with Woolworths in respect of leasehold sites. Similarly, while Coles' first preference is to lease sites, in those situations where it has purchased freehold sites, Coles is most commonly competing with Woolworths for the site. In addition, many new stores are opened by Coles or Woolworths in undeveloped urban regions or growth corridors where store development occurs in anticipation of population reaching sustainable levels. Coles does not typically see ALDI, IGA or other independents enter these locations until population is well established, again, meaning that Coles is typically competing with Woolworths in relation to these greenfield site opportunities.

While Coles does not consider access to sites to be a material barrier to entry or expansion, Coles is supportive of changes to planning and zoning laws which would streamline processes, reduce conflicts between state and local planning regulations and reduce the overall time period that land would need to be held until it could be developed.

¹ See ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 145.

(d) Vigorous competition with Woolworths

While each competitor brings their own competitive strengths, Coles notes that the ACCC is particularly focused on the level of competition between Coles and Woolworths given their similar formats and breadth of store network. As anyone who has worked at a major supermarket chain can attest, the competitive rivalry between Coles and Woolworths on all fronts is fiercely intense. For many years, Coles has targeted lower prices than Woolworths at an overall supermarket level. Moreover, a review of competition since the ACCC's 2008 Inquiry reveals not only vigorous day to day competition, but very substantial investments in value, store renewal and supply chain modernisation over the years as each major supermarket chain seeks to reset and refresh its strategy and lead sales growth. These investments are not discussed in the Interim Report but they are an important feature of how competition has occurred in grocery retailing, with Coles, Woolworths and other supermarket chains expanding their shares or falling behind depending on their investments in the customer offer, their store network and in supply chain modernisation.

(e) ALDI is a strong competitive constraint

Coles agrees with the ACCC's finding that ALDI is an important source of competitive constraint on Coles and Woolworths² but disagrees that ALDI provides only a partial 'price constraint'. A review of Coles' internal documents, which have been produced to the ACCC, demonstrates a very high degree of focus on ALDI's pricing and competitive behaviour. While ALDI's range is more limited, it has grown over time (especially in fresh produce and branded products), and areas of overlap generally include the highest volume staples that form a core component of a customer's shopping basket. In addition, while ALDI's network is not as extensive as Coles and Woolworths, Coles' pricing is generally consistent nationally, which means that the pricing constraint imposed by ALDI is not limited to those states or locations where it currently has stores. For example, Coles' pricing in Tasmania is the same as in Victoria and ALDI has no presence in Tasmania.

(f) Cross shopping imposes a significant constraint on supermarkets

The ACCC's Interim Report acknowledges that most consumers visit multiple stores during a typical week to do their grocery shopping and that other grocery retailers may impose a degree of competitive constraint on supermarkets where their offerings overlap.³

Coles agrees that the risk of customers splitting their baskets across supermarket retailers is a key competitive dynamic in the modern grocery environment that must be examined by the ACCC, particularly because it is facilitated by the collocation of supermarkets with specialty and category retailers as well as the increasing convenience of online shopping. However, there is no logical reason to restrict an analysis of basket splitting to supermarket retailers only. The ability and increasing propensity of customers to disaggregate their baskets across supermarkets, online retailers such as Amazon and Catch, category specialists such as Bunnings and specialty retailers such as greengrocers and butchers must be examined to ensure a fulsome picture of the competitive landscape. Coles is concerned that the Interim Report presents a relatively static view of competition with a potential bias towards the perspective of 'big basket' shoppers who might prefer a large single weekly shop in a bricks and mortar store, at the expense of the many other types of customers. A large number of customers shop multiple times per week, and have a greater propensity to shop online and at any number of different retailers in a shopping centre that compete in various product categories against the supermarkets.

The fact that Coles can lose custom not just to Woolworths, ALDI, Metcash and Costco, but also for some lines to other speciality retailers, further increases the competitive pressure.

Importantly, Coles submits that the ability of customers to disaggregate their spend across retailers imposes competitive tension not only in areas of product overlap. Rather, to remain a 'one stop shop' and win as much of the customer's basket as possible, supermarkets must offer customers a compelling proposition across the board, through value, range, location, convenience and service. Supermarkets are strongly incentivised to do so as they make higher and lower

² See ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 166.

³ See ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 153.

margins across different product categories and look to balance their return across the customer's shopping trip as a whole.

2.4 Supermarket profitability

The ACCC has indicated that it will consider supermarket profitability in the Inquiry because it can provide some insight into the level of competition within a market.⁴ The Interim Report focuses in particular on:

- Coles and Woolworths' EBIT margins over time⁵ (which are said to have increased);
- Coles and Woolworths' EBIT margins as compared to a selection of international peers⁶ (which are said to be more profitable than at least some overseas peers); and
- Coles' and Woolworths' return on capital (which is acknowledged to be broadly in line with international peers).⁷

While EBIT is undoubtedly an important measure for Coles' investor reporting and other purposes, Coles does not consider it to be the most appropriate measure for the ACCC's purposes of providing insight into the level of competition within the grocery sector. Coles considers NPAT to be a more appropriate measure for this purpose because it is an absolute profit calculation which considers all income and costs associated with running a business. NPAT is also the basis for dividend payments and CEO remuneration is linked to both Group EBIT and Group NPAT. Importantly, Coles Group's NPAT margin has remained relatively flat for the last five years, and since 2019, has decreased from 2.80 to 2.58%. Put another way, for every \$100 in operating revenue, Coles earned NPAT of \$2.80 in 2019 and \$2.57 in 2024.

In any event, Coles respectfully submits that the ACCC's finding that Coles' EBIT margins have increased over the last five years is incorrect. This is because the ACCC's analysis has not taken into account the adoption of Australian Accounting Standards Board 16 (AASB 16) in 2019, which changed the treatment of leases in calculating EBIT. These changes resulted in measures of EBIT (and EBIT margin) *increasing* compared to pre-AASB 16, because pre-AASB 16 reporting deducts the full lease expense from the calculation of EBIT whereas post-AASB 16 reporting deducts only depreciation of the right-of-use asset from the calculation of EBIT (and not interest on the lease liability). Coles leases the vast majority of the premises on which its supermarkets are located. It follows that a comparison of EBIT margins following the application of AASB 16 cannot be compared directly to EBIT margins before the application of AASB 16, as the ACCC does in its Interim Report, without considering the effect of these changes. Over the period analysed by the ACCC in the Interim Report, from FY18 to FY23, Coles' EBIT margins for its supermarkets segment increased by 0.9 percentage points, from 3.9% to 4.8%. This overall increase is less than the effect of AASB 16 on EBIT margin for the group, which indicates that the profitability margins of Coles' supermarket segment is unlikely to have changed materially over this period.

Finally, in relation to international comparisons, it is Coles' strong view that NPAT again provides a more appropriate profitability metric for the purpose of providing insights into the level of competition in the grocery sector and comparing businesses operating between jurisdictions. This is because NPAT considers all income and costs associated with running a business, whereas EBIT excludes key cost components such as interest and taxes. These can vary significantly between jurisdictions and can result in substantial differences in the actual earnings of a company.

⁴ See ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 191.

⁵ See ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 194.

⁶ See ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 197.

⁷ See ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 197.

3 Customer experience

3.1 Supermarket pricing

Coles seeks to offer customers strong value through competitive pricing, promotions and discounts, development of Own Brand as a quality, cheaper alternative to branded products as well as Flybuys rewards such as \$10 off payment redemption at the checkout.

As the ACCC has noted in the Interim Report, Coles has had uniform statewide pricing in place since 2010 which means that regional and metropolitan customers receive the same pricing offers regardless of location and the number of competitors in their local area. In practice, the vast majority of products are priced the same nationally. The state and nationwide pricing policies of the largest supermarket chains are facilitated by their scale and are a significant benefit to Australian consumers living in regional area as discussed further below. Coles also maintains consistent pricing across store formats (Coles Supermarkets and Coles Local) as well as between instore and online, with the exception of offering some additional online only specials.

Coles supports measures to enhance customer understanding of price competitiveness in Australia. This is because it is important not only for supermarkets to price competitively but for customer perception of price competitiveness to reflect the reality. Otherwise a customer's decision about where to shop can be distorted by inaccurate perceptions of where they can access the best value. For example, Coles has consistently targeted more competitive pricing than Woolworths at an overall supermarket level over the last five years. However, from time to time, Coles receives feedback from customer surveys which indicate that customers perceive Woolworths to offer more competitive pricing. For a similar reason, Coles supports more transparent disclosure of the products being compared by CHOICE in its government funded mystery shopping initiative. At present, customers have no way of assessing whether the products being purchased as part of these mystery shopping activities by CHOICE reflect comparable products in terms of price, quality and size.

(a) Regional pricing

One potential concern raised in the Interim Report is whether customers in regional areas pay higher prices for groceries than in metropolitan areas. Coles is acutely aware of additional difficulties that can be experienced by customers in regional areas, including greater fuel costs for longer shopping journeys and a greater reliance on sometimes fragile supply chains, which can result in more frequent out-of-stock situations or reduced product life on shelf.

As noted above, Coles has a statewide pricing policy (although in practice most products are priced the same nationally). One of the reasons this policy was introduced was to remove the perception that some regions were cross-subsidising others, and that some customers were winning at the expense of others. The only exception to Coles' statewide pricing policy is in relation to 13 stores located in more remote areas that apply an additional freight component into their retail pricing. These are 8 stores in the Northern Territory and 5 stores in WA. Some key value items such as meat categories do not have the same freight component applied and are priced the same across WA. Coles absorbs the higher costs of freighting these staples to these more remote stores.

On average, Coles classifies just over one third (around 36%) of its stores as regional, and just under two thirds as metro (around 64%).⁸ However, the additional freight component incorporated into retail pricing in more remote stores only applies to around 1.5% of Coles' store fleet. Coles notes that freight costs to these more remote areas are very significant. For example, regional NT stores are serviced from Coles' South Australian DCs. As an indication, the average cost per pallet to regional stores in NT via road (based on October 2024 fuel) was approximately 15 times higher than the metropolitan pallet rate in SA.

Finally, Coles notes that there are some extremely remote locations where Coles does not have any store presence but where Coles facilitates access to groceries by Indigenous communities. For example, Coles arranges for one team member in the Coles Casuarina store in Darwin to work full time to freeze and pack a range of groceries for transport for community members in remote locations across the top end of Australia, including on remote islands such as the Tiwi

⁸ This split may vary slightly over time with store openings and closures across the network.

Islands and Groot Eylandt. The price charged for these items is the same as for items in Coles' Darwin stores, plus a transport fee.

(b) Price comparison activities

The Interim Report notes that consumers are engaging in a higher degree of price comparison activity both before and during shopping.⁹ This is consistent with Coles' own research which suggests that a large number of customers engage in what is known as ROBI (Research Online, Buy In-store). This was a key reason that Coles invested in improving its digital offering so that customers had a smoother integrated experience between Coles' website, App and shopping in-store. 55% of Coles App users now utilise in-store mode. Coles has also implemented functionality into its website and App so that customers can filter search results by lowest to highest price, lowest unit price and specials.

Coles notes the ACCC's view that consumers' ability to rely on online sources depends on factors such as whether grocery retailers publish their prices online and whether the supermarket's pricing can be accessed by price comparison websites or apps.¹⁰ Coles publishes its pricing information online and its online pricing is consistent with in-store pricing (with the exception of some online only discounts). Coles' pricing data is also available to be 'scraped' by price comparison websites and apps.

If other grocery retailers published their retail prices online this would facilitate price comparison activities by consumers. There is unlikely to be any competitive detriment in doing so given that supermarket retailers already closely monitor and track their competitors' publicly available pricing, for example, through price checking activities in-store.

(c) CHOICE mystery grocery basket shop

As noted in the Interim Report, in 2024 the Australian Government commenced funding CHOICE to conduct surveys of supermarket prices across Australia through mystery shoppers and to provide quarterly reports on those survey results. The survey results are based on the following 14 grocery items sold in 27 locations across Australia and compare the price of supermarkets within 5 km of each other.

⁹ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, pages 82–3.

¹⁰ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 85.

Figure 1: Products purchased by CHOICE in supermarket survey

The CHOICE shopping list

Here is the full list of grocery items that we priced



- Apples
- Beef mince
- Bread, white, sliced
- Butter
- Carrots
- Cheese, block
- Flour
- Milk, full cream
- Peas, frozen
- Penne pasta
- Sugar, white
- Tea bags
- Tinned tomatoes, diced
- Weet-Bix
- Spotlight item: Washing powder (June 2024)

Source: CHOICE [website](#) accessed 11 November 2024

Coles' strong view is that CHOICE's mystery grocery basket shop could play a more meaningful role in educating customers about price competition if the actual brands purchased as part of the mystery shop were disclosed to consumers. Because ALDI primarily sells private label products, it is unclear at present whether CHOICE is comparing 'like for like' in the products selected. Publishing the products actually purchased would enable customers to review the results of the mystery shop themselves and assess both the quality and the price of the basket shopped.

In relation to this issue, CHOICE has stated:¹¹

In order to make the most accurate comparisons, many of the products in our shop come from national brands (such as CSR, Sanitarium and Lipton), which are sold in most, if not all, major supermarket chains. Selection of the products for each basket item is based on wide availability, and the closest comparable items are selected when these are not available.

Our basket included a mix of both house-brand and national-brand items. This was true for Aldi as well as Coles, Woolworths and IGA....

We also spend a lot of time in stores and online to make sure the items we choose are comparable – that means they need to be the same size and similar in product quality, as well as appearance.

Notwithstanding this, CHOICE has declined to disclose the specific products purchased as part of its mystery shop. It was reported that a CHOICE spokesperson indicated that "doing so would compromise the accuracy and integrity of the study".¹² It is very difficult to see how disclosing the products purchased after the mystery shop has completed could

¹¹ See CHOICE, *How we survey supermarket grocery prices*, 26 September 2024, <<https://www.choice.com.au/shopping/everyday-shopping/supermarkets/articles/how-we-surveyed-the-supermarkets>>.

¹² See Australian Financial Review, *Red flag over Choice's taxpayer-funded grocery price watch*, 11 November 2024, <<https://www.afr.com/companies/retail/red-flag-over-choice-s-taxpayer-funded-grocery-price-watch-20241104-p5knta>>.

affect the accuracy and integrity of the study and Coles strongly supports greater transparency in relation to CHOICE's mystery grocery basket shop.

3.2 Promotions

Coles offers a range of specials, discounts and promotions across Coles Supermarkets, Coles Local and Coles Online. Like regular pricing, promotional pricing is generally consistent nationally although promotional pricing for meat, beverages, tobacco and fresh produce occurs on a statewide basis.¹³

Promotional pricing is also virtually the same across Coles' different store formats, since over 90% of the products at Coles Local are also supplied at Coles Supermarkets and will have the same state-based promotional activity. Similarly, promotional pricing is the same between Coles Supermarkets and Coles Online, although Coles Online also offers some additional discounts to customers which are available online only.

Coles aims to offer a broad range of discounts and promotions that suit different customer needs. This includes short-term promotions or 'specials' (these comprise the majority of Coles' promotions); longer term price drop campaigns such as Down Down; and multi-saves where customers are offered savings for purchasing more than one item. Coles also offers Everyday Value which are not promotions but where prices are held at a low regular shelf price that customers can depend on.

Coles has listened to a range of ACCC and stakeholder feedback about promotions and sets out its response below.

(a) Clarity around promotional rules

As noted in Coles' response to the Issues Paper and in the Interim Report,¹⁴ the ACCC has published general guidance on avoiding misleading representations in respect of pricing and other claims such as 'was/now' pricing or percentage or dollar savings.¹⁵ Those guidelines suggest that when determining whether a represented saving will be achieved, a critical issue is whether relevant consumers would have paid the 'was' or 'strike through' price to purchase that item for a 'reasonable period' before the sale commenced. The guidelines do not provide any detailed guidance on what a reasonable period is and much of the case law in this area relates to occasional purchases such as furniture and jewellery, which have limited relevance in the grocery sector which involves fast moving consumer goods.

Because regulatory and judicial guidance is limited, grocery retailers currently formulate their own internal compliance guardrails regarding how often products can be promoted and how long the higher shelf price must be established before the price can drop and a discount be claimed. Coles previously submitted that both competition and consumer outcomes in grocery could be enhanced by the ACCC publishing more detailed guidance on pricing and promotional claims (this is referred to as Option 1 in the Interim Report). Coles notes that compliance guardrails of this kind must necessarily strike a balance between facilitating and restricting competitive pricing – the longer that the regular shelf price is established, the lower the risk that a discount claim will be regarded as non-genuine and therefore misleading, but equally, the less often the product will be discounted, therefore reducing price competition in the market.

As the ACCC has recently commenced litigation against Coles and Woolworths regarding one promotional type, it may be necessary for court outcomes to be considered as part of the development of additional ACCC guidance for the industry.

As noted in section **3.2 (b)** below, Coles is currently updating its own website to provide additional information to customers about its promotional types to assist customer understanding. Coles notes that more consistent compliance guardrails across industry would enable more consistent communications to customers about promotions and what they

¹³ There are a small number of stores that do not run any promotions for logistical reasons including the Sydney and Perth CBD stores.

¹⁴ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 78.

¹⁵ See ACCC, *Advertising and Selling Guide*, July 2021, <<https://www.accc.gov.au/system/files/Advertising%20and%20selling%20guide%20-%20July%202021.pdf>>.

mean. This would support enhanced consumer and competitive outcomes, as it would assist customers to better understand promotions but also better compare offers between retailers.

(b) Transparency of prices

Coles notes the feedback from some consumer groups and consumers that some supermarket promotions may be confusing. The ACCC has indicated in its Interim Report that it will be considering this issue further, including assessing a range of options to alleviate the concerns raised.¹⁶

As noted above at (a), Coles is currently updating its website to make it easier for customers to identify value across Coles' stores and understand the different promotional types such as specials and Down Down.

Coles is also looking at ways to better inform customers when there are major supply changes that will impact retail pricing. For example, Australia has many regions where there is a concentration of growers of particular produce owing to favourable soil and climate conditions in that location. Where severe weather such as hailstorms damages crops in a particular region, a large proportion of supply can therefore be affected which can lead to shortages. In some cases where product shortages occur and market pricing increases, this can also have a 'knock on' effect to other products and suppliers as customers trade out of higher priced produce and into cheaper produce that is in greater abundance, potentially leading to further stock shortages.

(c) Multi-buys

Another area of concern raised in the Interim Report is whether multi-buy offers support optimal consumer decision making and should be permitted, particularly on essential items. Multi-buys (where consumers receive a discount for purchasing two or more products) are one promotional type offered by Coles (comprising approximately 13% of promotions). Coles seeks to cater for a wide range of customers in its ranging and pricing decisions. Not all offers will appeal to all customers.

Coles does not support policy measures which would in effect restrict price competition between retailers. Coles considers that multi-buys offer strong value to customers who are willing to purchase in larger volumes in order to access discounted prices, and they are one way that Coles competes with Costco, Bunnings and other grocery retailers who sell bulk offers. Coles offers many other discounts that apply to purchases of a single unit.

Multi-buys are also an important promotional mechanism for suppliers to assist them to sell greater volumes of their products, including where the supplier might have an inventory management issue that can be assisted through this type of activity.

3.3 Shrinkflation

Like other product specifications, the weight or mass of a product is ultimately a matter for the supplier to determine as part of overall product design (although Coles must agree to proposed changes in respect of Coles Brand products). Coles' experience is that suppliers may change the product or mass of a product for a number of reasons, including standardising pack sizes within a range or to drive production efficiency. More recently, they have increasingly done so to respond to rising production costs. Coles understands and acknowledges customers' concerns with changes in weight or pack size, particularly for critical household items in the current economic climate. In recent years, where a proposed change in weight or pack size was driven by rising input costs, Coles' Category managers have typically sought to validate the increases in input costs against publicly available information under the process outlined in Coles' Cost Price Adjustment Policy.

Coles has approximately 6,000 Own Brand products, and aims to keep the size of Own Brand products as stable as possible to ensure consistency for our customers. In the past 12 months, changes have been made to the packaging size of only 30 Own Brand products, comprising 0.5% of the Own Brand product range. While Coles is not in a position to comment on the decisions of other suppliers with respect to product weight and size, Coles notes that where suppliers

¹⁶ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 78.

are facing genuine rising production costs, they may regard a change in weight or pack size as one measure they can take to manage these costs, in addition to reducing other costs or seeking to increase efficiencies in their manufacturing. This is because the alternative may be to seek cost price increases (which are likely to then lead to retail price increases) and some customers may consider that a reduction in weight or pack size is preferable to price increases.

Coles appreciates that customers can be frustrated by pack and weight size changes. In addition to the information already available to customers on pack and on ticketing (in particular, the weight and size on pack and on shelf ticket and the unit price on shelf ticket), Coles is open to exploring measures to enhance customer transparency in this area as part of an industry wide solution. It will be important that potential impacts to suppliers are carefully considered. One reason why Coles has not unilaterally introduced notifications in respect of pack size and weight changes is due to concerns about potential compliance concerns under the Grocery Code and the impacts to its supplier partners.

3.4 Unit pricing

Coles considers that unit pricing assists customers to compare prices both in-store and between supermarkets and takes compliance in this area seriously. The results of the ACCC's consumer survey that 89% of respondents 'always' or 'usually' use unit pricing¹⁷ are consistent with Coles' own experience.

Coles notes the Australian Government's recent announcement (following the release of the ACCC's Interim Report) that it will be consulting on potential changes to the Unit Pricing Code. The Government has indicated that consultation will canvass changes to the Code such as:

- improving readability and visibility of unit pricing in stores;
- addressing inconsistent use of units of measure across supermarkets;
- whether to expand the scope of retailers covered by the Code;
- more specific prominence and legibility requirements; and
- improving the use of unit pricing in cross-retailer price comparisons.

Although the Unit Pricing Code was only recently reviewed in 2021 and found to be operating effectively at that time,¹⁸ Coles welcomes the review and will be participating in the consultation. Coles is supportive of requiring greater consistency with units of measures and that a broader range of retailers be covered by the Code (subject potentially to a minimum size threshold). Coles is also open to more specific prominence and legibility requirements although it will be important that any new requirements can be operationalised in practice, including with respect to the information already required to be placed on ticket, electronic labels and overall legibility and clarity.

3.5 Loyalty

Coles agrees with the ACCC's finding that loyalty programs are an important aspect of competition in retail.¹⁹ Flybuys is one way that Coles delivers value to customers, including through the collection and redemption of Flybuys points for goods or services or through instant cash-off offers at the Coles check-out. Coles wants customers to clearly understand the benefits of its loyalty programs so that they can identify the value of each program, and is continually looking for ways to make customers more aware of the benefits that are available to them. For example, beginning in November 2020, Coles rolled out automatic prompts at the point of sale that inform a member when they have at least 10 Flybuys Dollars available and give them the option to redeem them. This has resulted in roughly a three-fold increase in the number of customers who redeem points on a weekly basis and redemption rates have continued to grow. In FY24,

¹⁷ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 14.

¹⁸ See Treasury, *Consultation on Competition and Consumer (Industry Codes - Unit Pricing) Regulations 2021*, June 2021, <<https://treasury.gov.au/consultation/c2021-174950>>.

¹⁹ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 105.

there was a 57% increase in points redemption by Coles' customers and over 2 million members redeemed points for the first time at Coles.

However, while loyalty programs such as Flybuys deliver tangible benefits to consumers, they ultimately only form one aspect of competition between grocery retailers. Other factors such as overall value, product range, price and convenience are important drivers of customers' choice of supermarket. For this reason, Coles does not consider that loyalty programs create barriers to entry or expansion for competing supermarkets. Indeed, consistent with the ACCC's consumer survey results, Coles' internal research suggests that the majority of Flybuys members are members of multiple loyalty schemes.

In aggregated form, the data collected through Flybuys enables Coles to improve its overall offering for customers, including by informing ranging decisions and placement of products in store and assessing the effectiveness of promotions. In non-aggregated form, Flybuys data can also provide direct benefits to members such as personalised offers and provision of information about product recalls or customer refunds.

Coles agrees that it is critical that members are informed about how their data may be used when they sign up to become Flybuys members. Coles has robust systems and processes in place to ensure it collects, uses and retains personal information in accordance with privacy laws and robust data security standards. It is important to note that Coles' Flybuys loyalty program has an express opt-out for members in relation to targeted advertising, both generally and in relation to certain products or brands. The provision of Flybuys data to third parties is clearly set out in the program Terms and Conditions. Where it is shared with third parties, it is for a particular purpose (for example, to provide suppliers insights in relation to their product performance), and done so in an aggregated and anonymised manner.

3.6 Team-member assisted check outs

Coles notes feedback from some consumer groups about the use of team-member assisted checkouts where customers can check out their own groceries with the support of team members on hand to support in dedicated areas.

As part of a Service Transformation project, as well as new store and renewal layouts, Coles consistently re-assesses the proportion of checkouts in stores that are full service relative to team-member assisted checkouts. This does not mean that Coles is employing fewer staff – in contrast, Coles is employing more team members around the country than ever before, with checkout efficiencies supporting investment into servicing other channels, such as digital.

When making decisions about the composition of checkouts in any given store, Coles considers a range of factors including customer satisfaction, customer density, customer basket size and operating efficiencies. Service refurbishments are underpinned by data analysis that aims to minimise customer wait times, enhance the overall shopping experience and ensure efficient operations. In particular, Coles monitors transaction data for each individual store with a view to ensuring that the right number of team members are supporting each individual store at their busiest times. Service Transformation has significantly increased the capacity of store check-outs at the front of store, reducing wait times for customers during busy periods.

Customer Service Managers and Store Managers have discretion to use their localised knowledge to manage the particulars of their workforces within guidelines. This is an important part of workforce optimisation as sometimes the busyness of an individual store can be impacted by things like changes in weather, nearby recreational events and other local factors.

4 Suppliers

Coles agrees that efficient supply chains are crucial for ensuring markets for the supply of groceries are working well for consumers, suppliers and the Australian economy.²⁰ Building successful, sustainable relationships with suppliers is critical to Coles' business and many of Coles' supplier relationships are longstanding, with some lasting more than 50 years in fresh produce and more than 20 years in meat, dairy and grocery.

²⁰ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 207.

Coles has made significant investments in the trading relationship with its suppliers, launching its own Supplier Code in 2014 and voluntarily becoming a signatory to the Grocery Code in 2015. While Coles considers its relationships with suppliers to be generally strong, Coles looks to continually improve its processes to support positive and sustainable business relationships with all trading partners, including through regular supplier satisfaction surveys which are presented to Coles' senior leadership such as the Advantage Voice Survey and the Grocery Code Survey.

While the ACCC has not yet formed a view on the concerns raised by suppliers, Coles responds below to a number of concerns that have received a particular focus in the Interim Report. Fresh produce suppliers in particular have raised concerns about aspects of supermarket operations that they believe could be improved, including greater transparency and additional information to assist them in their decision making when supplying to supermarkets. Coles is committed to continuous improvement of its business and the sector and welcomes further engagement regarding proposed solutions to the matters raised.

4.1 Fresh produce suppliers

As Coles identified in its response to the Issues Paper, the procurement of fresh produce is more complex than in other perishable supply chains such as meat and dairy. In Coles' view, this is because the supplier base is highly fragmented, production can be affected by variable weather conditions and consumer purchasing patterns can change quickly (e.g., customers may trade from one product into another in response to changes in prices). All of these factors combine to make it more difficult to predict volume requirements and market prices for fresh produce. This can be contrasted to other fresh supply chains such as beef and pork where Coles is able to source nearly all of its requirements through forward contracts and where volumes and price are agreed up front.

(a) Fresh produce volumes

Coles notes the concerns raised by some suppliers about the accuracy of volume forecasts that are provided by supermarkets to suppliers at the start of the growing season. The ACCC has indicated that it will consider the extent to which suppliers relying on these forecasts to inform growing decisions may result in oversupply and advantage the supermarket by placing downward pressure on the price for which supermarkets could source the product.²¹

The volume forecasts that Coles provides to suppliers at the beginning of each growing season reflect Coles' best estimate of what it will acquire from that supplier over the season, based on what Coles considers it can reasonably sell to customers at a total category level. Coles has no incentive to 'over forecast' as Coles commits to purchasing these volumes from the supplier, subject to a 15% variation up or down which provides flexibility for both Coles and the supplier such as in the event of crop challenges or shifts in customer buying behaviour.

To prepare the volume forecasts provided to individual suppliers, Coles category teams formulate an aggregate volume forecast for the category based on factors such as the volumes sold in the prior two years, seasonal conditions that may impact crop yield and other relevant factors (such as year on year sales growth or changing customer preferences in respect of that product). Category teams may also seek information from growers on their expected yields for the upcoming growing season to understand the total volumes that may become available in the market. This is because greater availability of product will drive lower cost and therefore lower retail prices which drives demand. Conversely, supply constraints will drive higher cost and therefore higher retail prices which can also suppress demand.

Once the overall category forecast is set, the category teams develop a volume forecast of what proportion of that demand Coles expects to buy from each supplier by state. This is known as the 'split' for each supplier. The splits then form the basis of the commitment provided to each supplier and are entered into Coles' ordering system. For competition law reasons, Coles only provide each supplier with information about their own volume forecasts. Coles does not provide suppliers with the volume forecasts of their competitors.

²¹ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 236.

While Coles uses all available data to prepare as accurate volume forecasts as possible, predicting consumer demand is inherently difficult. It is for this reason that both Coles and the supplier agree to use all reasonable endeavours to keep the other party updated on any circumstances that may impact the forecast or the ability to meet the forecast.

Where consumer demand is higher than expected and suppliers have additional produce available, suppliers will typically receive greater orders than what was forecast prior to the growing season. Where Coles orders fewer volumes from suppliers than what was forecast, there can be a range of reasons, such as reduced consumer demand due to consumers trading into alternative products or retail price inflation driven by increases in wholesale cost. Sometimes suppliers do not have product available due to crops being damaged by weather events or growing seasons finishing earlier than expected.

Coles acknowledges the concerns raised by growers in this area which Coles believes are exacerbated by information asymmetries and a lack of transparency at various points in the supply chain, particularly when growers sell via aggregators rather than direct to supermarkets. Coles is examining ways in which it can improve the current ordering and volume commitment process to enhance transparency and reduce situations in which there are significant changes in volumes than those agreed prior to the growing season.

(b) Fresh produce prices

Coles notes that some suppliers have raised concerns about a lack of transparency in the weekly negotiation process for fresh produce, specifically, that supermarkets have full insight into the volumes and prices that all suppliers bid each week but that individual suppliers do not have access to any information except their own.²²

The price of fresh produce is generally agreed on a weekly basis. Suppliers provide the prices and volumes they are willing to supply that week through an online portal and Coles negotiates with each supplier having regard to the bids place by other suppliers and/or by reference to the central market price for that product. The central market price is available via Ausmarket data (www.ausmarket.com.au), a widely used subscription service that contains pricing data for produce sold in the central markets of Adelaide, Brisbane, Melbourne and Sydney. Some suppliers supply to multiple retailers, and in those cases, have broader visibility of prices across the market.

The market price goes up and down depending on a number of factors, but weather conditions (and increasingly weather events such as drought, floods and heatwaves) are particularly impactful. Favourable growing conditions will lead to products being in 'flush', pushing market prices down (and leading to lower retail prices). Conversely, unfavourable growing conditions and climate events can drive significant increases in market prices. Unfavourable growing conditions can be both short term (affecting produce available to harvest at the time) as well as long term (for example, impacting the ability to sow a crop that affects future produce availability). Coles notes that if Coles were to accept higher prices from suppliers during periods of flush, customers would likely seek out cheaper prices from other retailers.

Prices and volumes are typically agreed on a Tuesday and suppliers receive Purchase Orders on Thursdays outlining the agreed price and volume for the following week. Suppliers are able to lock in the Purchase Order at that time, in which case prices and volumes are firm, however Coles' experience is that suppliers typically leave the Purchase Order open unless they wish to pack early (eg, ahead of a public holiday). In some cases, this is because the supplier wants the option to negotiate to add more volume to the purchase order.

Coles acknowledges the concerns raised by growers in this area. For competition law reasons, Coles cannot provide growers with information about the bids of competing suppliers. However, Coles welcomes a discussion on areas for improvement, including potentially through centralised publication of pricing and volume data to assist growers with their planning.

²² See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 236.

(c) Quality assurance

One concern raised by stakeholders is whether quality assessment and rejection processes are being used for purposes other than genuine quality issues, including to manage the volumes supermarkets receive.²³

Coles acknowledges that it can be particularly difficult for suppliers when fresh produce is rejected, especially where the quality issues are due to weather events beyond the control of the supplier. However, Coles has found no evidence of produce being rejected for reasons other than genuine quality issues.

It is important to conduct rigorous quality assurance over fresh produce to ensure produce sold in its stores meets consumer expectations. The quality team who conduct those assessments are independent of the fresh buying team and have no role in formulating forecasts or placing orders with suppliers. The process is also independently audited and reviewed by a third party. Coles has rigorous processes in place to ensure thorough, consistent and fair testing of product. In particular:

- Given the volume of fresh produce received at a DC on a daily basis, it is not possible for Coles to review every unit of produce it receives. Instead, Coles adopts a sampling model.
- The number of crates that are selected for inspection is determined by Coles' Sampling Plan. For example, the Sampling Plan provides that, if a consignment of fresh produce contains up to 100 cartons, then five crates, cartons or boxes (as the case may be) will be selected for inspection. The Sampling Plan is based on international standards and designed to deliver a statistically significant result that is representative of the entire delivery.
- Once a consignment is selected for assessment, the first assessment is a temperature check from the centre of the pallet.
- A random sample of cartons from different sections of the pallet are then selected for assessment to ensure a fair representation of the product.
- The inspector then assesses the selected cartons against each criterion in the relevant specifications and the results are recorded electronically in a QAS report using a red, amber and green framework.
- If products are assessed as amber or green, they are accepted by Coles and released for picking and distribution to stores. If products are assessed as red, Coles undertakes a further quality check using a different sample and an increased sample size.
- If products are assessed as amber or green after retesting, products are released for picking and distribution to stores. If products are again assessed as red after retesting, the results are reviewed by a supervisor and then, if confirmed, notified to the supplier within 1 – 2 hours. Where product is assessed as red, the order received from the supplier is rejected.
- All produce that has been rejected through this process is set aside in the DC and the supplier is contacted by the Quality Inspector for instructions on what to do with the produce. Suppliers may choose to pick up the rejected produce and re-sell it on central markets or opt to have it donated. Suppliers may also take this opportunity to raise concerns about the rejection and these issues are resolved between the Category teams and the supplier.
- From time to time, produce may be 'conditionally accepted'. Conditional acceptances refer to circumstances where Coles flags produce in the system as being non-compliant with the applicable product specification but still accepts the goods for sale in stores. There are typically around three conditional acceptances raised each week. Conditional acceptances are decided on a case-by-case basis. One situation where this may occur is where there has been a failure to meet the qualitative requirements in the specifications early on in the growing season where it is unclear if specifications may change and where the non-compliance isn't considered serious enough to justify rejecting the goods.
- Suppliers can request a temporary 'variation' to the specification from Coles in circumstances where growing conditions or season timing or length in their region have impacted their ability to meet all parameters of the

²³ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 239.

specification. For example, persistent cloudiness and rain will make strawberries softer and less sweet, and will also slow ripening; excessive rain will increase the possibility of rots and mould growth, leaving the berries unfit for sale. Coles carefully considers variation requests to balance fairness to suppliers with suitable quality for customers.

- A number of suppliers already visit Coles' DCs periodically to better understand the quality checking process (in the six months prior to this submission, Coles hosted approximately 30 supplier visits across its DC network). From time to time, Coles may also offer other opportunities to Suppliers that provide insights into the process. For example, Coles recently hosted a webinar open to all Suppliers that demonstrated the quality checking process.

Coles' experience however is that its supplier partners generally supply very high quality produce in accordance with the agreed specifications and that rejections are relatively uncommon. For example, in FY23, Coles rejected just 1.49% of the fresh produce cartons it received from suppliers. In addition, where produce is rejected, Coles' product technologists work with suppliers with a view to preventing quality issues from recurring.

(d) Packaging

Coles notes that some fresh produce suppliers have raised concerns about supermarkets' packaging requirements, specifically, that they prevent suppliers from seeking to establish brand awareness or brand loyalty and that packaging requirements make it more difficult and costly for suppliers to seek to sell rejected stock through other channels once produce has been packed and branded to the supermarkets' requirements.²⁴ When developing packaging requirements, Coles considers a number of factors, including:

- **Protection of product:** one purpose of packaging is to protect the product during transit, both from the supplier to Coles and from Coles to the customer's home. For example, salad leaves are packaged in sealed plastic bags to minimise the risk of contamination, and berries are packaged in plastic punnets to avoid them being crushed or contaminated.
- **Shelf life of product:** the type of packaging used can extend (or reduce) a product's shelf life. For example, continental cucumbers are shrink wrapped in plastic because it significantly extends their shelf life.
- **Sustainability:** in line with customer expectations, Coles has significant sustainability commitments, as described below. For example, Coles worked with its suppliers to understand the practical transition of its secondary packaging requirements for iceberg lettuces from waxed cardboard boxes to Returnable Plastic Crates (**RPCs**), as the waxed cardboard boxes could not be recycled. Our suppliers have aligned to transition to using RPCs in this example.
- **Traceability:** packaging allows a supplier name to be placed on the product, and in some cases, contains a Global Identification Item Number (**GTIN**) barcode that links the fruit to a packing shed, to assist in traceability.
- **Safety:** packaging requirements may be for the purpose of safety considerations (e.g., to ensure that the product is not too heavy when it is stacked on the shelf).
- **Layout:** shelf-friendly packaging (i.e., cases designed to be opened and displayed on the shelf) needs to fit in the shelf space available.
- **Visual appearance:** packaging assists a customer in knowing what the product is and provides a barcode for scanning for ease of purchase.

Coles is a signatory to the Australian Packaging Covenant and a member of the Australian Packaging Covenant Organisation (**APCO**), tasked with facilitating the delivery of Australia's 2025 National Packaging Targets. Coles is also a founding member of the Australia New Zealand and Pacific Islands Plastics Pact (**ANZPAC Plastics Pact**). Coles is working towards the following for Coles Own Brand packaging:¹²

- reducing excess packaging where possible and ensuring the packaging remains fit for purpose;
- utilising packaging that is recyclable, reusable or compostable;

²⁴ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 207.

- phasing out problematic, unnecessary, and single-use plastics packaging;
- supporting industry to achieve an average of 50% post-consumer recycled content across packaging and 25% post-consumer recycled content across plastic packaging; and
- phasing out PFAS (Perfluoroalkyl and Polyfluoroalkyl Substances) from all fibre-based packaging.

Coles' packaging requirements are provided to all suppliers and available on Coles' Supplier Portal.

Generally, Coles does not provide suppliers with packaging or require suppliers to acquire packaging from a specific supplier. For packaging (other than Coles Own Brand packaging) (e.g., cardboard cartons for pre-pack apples), the product specifications and FPSA contain the requirements for the packaging. Suppliers then select the company of their choice who can provide the packaging according to those requirements.

For all Coles Own Brand products (including fresh produce), to maintain a consistent look for the Coles range of goods, suppliers are required to use the design and artwork for packaging as supplied by Coles. Suppliers are able to use a printer of their choice, provided the printer meets Coles' Approved Printer Audit specifications and completes a Print Requirements Form. Coles will provide the supplier with the artwork for the supplier's preferred printer's specifications.

For products that are proprietary branded (e.g., Jazz apples, Calypso mangos, Zespri kiwifruit and Qukes (baby cucumbers supplied by Perfection Fresh) or exclusive to Coles (e.g., Eureka blueberries and Perino tomatoes) there are no restrictions on suppliers applying their own branding to fresh produce supplied to the Supermarkets Business. In relation to the PLU stickers for loose fresh produce, suppliers are not prevented from including their name or branding on the PLU stickers and a number of growers/packers do include their name and branding on the PLU sticker.

In some instances, the artwork on a Coles Brand fresh produce item may be specific to a particular grower. For example, the Coles 1kg carrot pack currently features specific growers on the products they each pack.

4.2 Other services available to suppliers

Coles notes that some suppliers have raised concerns about requirements to use services provided by supermarkets or third parties nominated by supermarkets, including in relation to packaging of produce, freight, advertising and marketing and accreditation and auditing.²⁵

Coles offers a number of ancillary services to suppliers which they can acquire if they wish to do so. These services offer benefits to suppliers and facilitate efficiencies at various points of the supply chain. While Coles recommends using these services to suppliers where relevant, they are entirely optional.

(a) Coles Crates

Fresh produce suppliers have the option to use reusable crates when supplying products to Coles. The key benefits of Coles Crates are reducing cardboard waste in the context of the environmental impact of both Coles and its suppliers, as well as efficiency and safety benefits. The standardised footprint and strong, interlocking design of reusable crates, as well as the better protection they offer fresh produce relative to single use packaging, improves efficiencies throughout the supply chain.

Coles Crates are owned and managed by a third party provider and operate as a pooling asset:

- Produce is packed into crates by suppliers and delivered to Coles;
- Coles unloads the products from the crates;
- The third party picks up the crates from Coles' DCs and washes them; and
- Suppliers can either pick the crates up from the washing facility or have the third party return them to the supplier.

²⁵ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 242.

The service is optional, and some suppliers choose not to use Coles Crates due to the nature of their product or the cost. For example, banana suppliers generally do not use Coles Crates as these products travel well in cardboard boxes which are more flexible next to the fruit.

(b) Coles Collect

Coles Collect is an in-house national freight solution provider which manages the transportation of suppliers' goods into Coles DCs and, in limited circumstances, back to suppliers in the event that a delivery is rejected for quality reasons.

Coles Collect transports all commodities, including fresh produce, frozen, packaged products and liquor. Coles Collect also provides some freight services to other retailers like wholesale fresh produce markets.

Coles Collect is optional for suppliers. It is used by suppliers of all sizes and scale (including small suppliers without logistics or supply chain experience who may otherwise find it difficult to move their products in a cost effective way).

The scale of Coles' operations and extensive distribution network means it is able to offer suppliers a competitive offering. Typically, suppliers assess Coles Collect along with other providers in a competitive tender process and rates are negotiated on an individual basis.

Coles Collect manages also contingency planning for events like floods, fires, COVID-19 or rail outages.

(c) Coles 360

Coles 360 is a retail media business owned by Coles Group that supplies marketing services to both Coles and suppliers. This includes advertising products in channels such as Coles Online, Coles Magazine, Coles Digital Screens, Coles Radio and extending into other media partners (e.g., Meta and YouTube). Coles 360 may work directly with suppliers to plan marketing campaigns using each of these channels. Coles 360 provides suppliers with media assets (such as Coles Radio, digital displays and floor decals).

Coles 360 employs an independent third party to benchmark pricing by reference to audience, performance and other metrics on a six monthly to annual basis. The third party benchmarks the rates cards to ensure it is competitive in market.

There are many alternative marketing avenues open to suppliers other than Coles 360.

(d) Supplier data analytics (eg, Coles Synergy)

Coles provides all its suppliers with access to sales, profit, item forecast and DC performance metric data for their own business at no cost, via Coles Supplier Central.

Suppliers seeking a broader range of data have the option to subscribe to Coles' data in the Coles Synergy platform, which is provided by Circana (a third party analytics and technology provider to retailers globally). This subscription grants access to a more extensive set of metrics that provide suppliers with the ability to see their own product performance in Coles benchmarked against other suppliers' in relevant categories and sub-categories. The pricing for the subscription is dependent on the size of the supplier, with larger suppliers paying more. This ensures that cost is not a barrier for smaller suppliers, and consistent with this, Coles has seen growth in adoption among small-to-medium suppliers.

The Coles Synergy model is typical of that used across the retail sector, among many Australian and global retailers. The availability of these insights helps suppliers make data-driven decisions, ultimately leading to better outcomes for suppliers, customers, and Coles. Access to shared data strengthens Coles' collaborative relationships with suppliers, enabling both parties to work together to optimise product offerings, enhance customer experiences, and drive innovation in the Australian grocery sector.

(e) Third-Party Audit Program

Under Coles' Ethical Sourcing Policy, Coles takes steps to ensure that the products it sells are produced and sourced in compliance with the law, which includes being assured that workers in the supply chain are working in safe environments, are paid correctly and their basic human rights are protected. This is critical to Coles being able to understand, as is required under the *Modern Slavery Act 2018* (Cth), potential modern slavery risks in Coles' supply chain.

Suppliers that are required to comply with the Ethical Sourcing Policy are suppliers of fresh produce, Coles Brand product and certain goods-not-for-resale suppliers.

As part of our ethical sourcing program, suppliers complete a risk assessment. Suppliers who receive a medium or high risk outcome need to undertake an ethical sourcing audit to ensure their operations meet basic social compliance requirements. These audits check things like fire safety compliance, availability of appropriate PPE and correct payment of wages. The criticality of audits is demonstrated through the regular identification of critical and major non-conformances across suppliers, including those in the agricultural sector. These non-conformances are often for concerning business and site safety issues, inclusive of general health and safety, underpayments, fire safety, and excessive working hours.

In the last financial year, 5,190 critical and major non-conformances were raised across our in-scope suppliers in Australia, with the key matters of concern identified falling in the categories of:

- Health, safety & hygiene
- Incorrect wages
- Excessive working hours

More than 50% of critical and major non-conformances were in the health, safety & hygiene category. Of these, fire safety issues accounted for almost 40% of the issues identified, with other non-conformances related to items such as dangerous chemicals, electrical risk, machinery risk, PPE concerns, poor accommodation / living conditions having repeated findings.

Despite the routine identification of the above issues, Coles recognises there is a cost associated with auditing and has been conscious of the need to enhance the number and experience / qualifications of auditors in the Australian market. To address the gap, over the last three years Coles has wholly funded over \$3.79 million worth of audits in the agricultural sector so costs are being shared with our supplier base as they become more familiar with the auditing program. Through investing in key audit partners in Australia, Coles has provided surety of future business, and facilitated a scheme where auditor numbers have increased, as have the qualifications of many in the market. Additionally, through Coles covering the cost of initial audits, where the more serious matters are being identified usually for the first time, and businesses are adapting to the requirements of an auditing process, it is anticipated the costs for suppliers associated with follow up audits and verification activities to close out critical and major non-conformances will be avoided or reduced in the future following improvement in their business practices.

4.3 Rebates

Coles notes concerns raised by some suppliers that rebates lack transparency and that they do not understand what benefit they receive from paying them.²⁶

Trading terms such as volume rebates and settlement discounts are largely a historical feature of the supermarket industry which enabled suppliers to have a consistent cost or list price with their customers but then provide certain larger customers such as Coles additional rebates for things like the inherently larger volumes (e.g., volume rebates), the benefit of supplying to DC rather than stores (DC Allowance) and benefits of creditworthiness, lower counterparty risk, improved administrative processes or more favourable payment terms (e.g., Settlement Discount).

Rebates are typically negotiated at the start of the trading relationship, recorded in writing in accordance with the Grocery Code and clearly specified on payment summaries / remittance documents.

²⁶ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 241.

4.4 Cost price increases

One concern that has been raised by some suppliers of packaged product is whether they have an effective ability to negotiate cost price increases with the major supermarket chains.²⁷

The cost of goods is a major driver of the retail price. To keep retail prices low, it is therefore critical for supermarkets both to negotiate competitive cost prices and to validate requests for cost price increase requests to ensure that they are appropriate.

In its recent submission to the Inquiry, the AFGC refers to the 'inability, over the preceding decade, of suppliers to reliably secure wholesale price increases for their products'. The AFGC submissions includes a graph which suggests a divergence between the rising input costs of AFGC manufacturers and the prices paid for their product. They submit that 'input costs to food manufacturing (such as agricultural commodities, transport and energy prices) rose at double the rate of output prices'.²⁸ To the extent the AFGC's submission suggests that Coles has not accepted cost price increases from suppliers in the last 10 years, that submission is not correct. Coles assesses all cost price increase requests in accordance with its cost price adjustment policy and it has not been Coles' experience that suppliers cannot successfully negotiate cost price increases. In analysis Coles has conducted for cost price increase requests in the last 5 years, Coles has accepted over 90% of the value of the cost price increase requests received from suppliers, including \$3.88 billion in price increases from packaged suppliers since FY22.

Coles assesses all cost price increase requests in accordance with its cost price adjustment policy and it has not been Coles' experience that suppliers cannot successfully negotiate cost price increases.

Price increases are also regulated by the Food and Grocery Code of Conduct:

- Retailers must notify suppliers within 30 days of whether Coles accepts, partially accepts or does not accept a proposed cost price increase.
- The supplier may request the retailer to enter negotiations.
- The retailer must negotiate in good faith and take all reasonable steps to conclude the negotiation without delay.

The ability of retailers to review cost price increase requests is an important part of supporting an efficient supply chain and keeping retail prices as low as possible. As the ACCC observes in the Interim Report:²⁹

"Bargaining power of supermarkets is efficiency enhancing, as its exercise can counteract seller market power and push wholesale prices closer to competitive levels. Regulators must therefore exercise caution when assessing buyer-side market power, to avoid misclassifying efficiency enhancing bargaining power as economically harmful monopsony power." [emphasis added]

During cost price negotiations with suppliers and the cost validation process, Coles does not require suppliers to submit commercially sensitive information.³⁰ Further, suppliers are given the option to engage an independent third party to conduct a confidential review of their request using Coles' review methodology.³¹

²⁷ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 233.

²⁸ See Australian Food and Grocery Council, *Interim Report Response*, October 2024, <https://www.accc.gov.au/system/files/AFGC_Final_0.pdf>.

²⁹ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 47.

³⁰ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 239.

³¹ See Coles, 'Coles Cost Price Alteration Policy', Supplier Central (Web page, 17 March 2023), <https://colessupplier.my.salesforce.com/sfc/p/#5j000001xFLw/a/5j000000dzTQ/Mrt6OWC2SKFPxfBklzNckd3JdXyHZSFC_zKowKYivE>.

4.5 Delisting decisions

A related concern raised by suppliers in the Interim Report is the potential for supermarkets to initiate delisting discussions during pricing reviews to obtain financial benefit.³²

Coles works hard with suppliers to constantly improve its value offer to customers. Product ranging is generally determined through Coles' formal range review process. Range reviews present an opportunity for Coles to (a) review the category strategy, (b) align its range to consumer preferences, (c) address inefficiencies in its current range (e.g., duplication and complexity) and (d) work with suppliers to develop plans for the year ahead that deliver on its mutual growth ambitions. Delisting products – through which products which are poor performing, duplicative etc - is an important part of maintaining dynamic efficiency of the supply chain.

Delisting decisions are also regulated by the Food and Grocery Code of Conduct:

- Retailers may only delist a supplier's grocery product in line with the relevant supply agreement and for genuine commercial reasons.
- Retailers must give reasonable written notice to the supplier before they delist a product.
- The supplier may ask for a review of a delisting decision.

Coles always seeks to use an objective criterion in making a decision to delist a product. These objectives are always pro-consumer. For example, common reasons for initiating delisting discussions with suppliers is the need simplify a complex range offering or introduce new products or innovative suppliers into the supply chain.

Coles notes Treasury's consideration of Grocery Code revisions following the Emerson Review. Coles believes that the current proposal to reverse the onus of proof such that normal commercial activities like making a decision to delist a product will be assumed to be an act of retribution against a supplier will have negative impacts on the efficiency of contracting, and make it more likely for retailers to seek supply from larger suppliers where displacing this assumption will be easier. We believe that a well-defined Code needs to strike the right balance between the fair treatment of suppliers and sustained best value for consumers.

4.6 Promotions

Coles notes that some suppliers have raised concerns about the way promotional activities are funded, including that suppliers may be asked to agree to fund a promotion at short notice.³³

As well as providing consumers with strong value, promotions on supermarket products provide important benefits to both retailers and suppliers. For suppliers, this includes substantially increased volumes, promotion of their brand and providing customers who have not tried their product with an opportunity to purchase it at a reduced price which potentially creates customer loyalty for the product going forward. Because of the benefits to suppliers, funding of promotions is commonly shared between Coles and its suppliers. In FY24, Coles contributed the majority of funding to the overall costs of price reductions on packaged product. The proportion funded by Coles has increased overall since 2019.

Products on promotion are sometimes placed on Promotional Ends (i.e., at the end of an aisle). They may also appear in Coles' catalogue. Suppliers do not typically pay to appear in these locations. In FY24, an average of only 10-20% of approximately 300 catalogue spaces per week were funded by suppliers, while an average of 20-30% of Promotional End placements were supplier funded. When making decisions about what products to feature in the catalogue or on Promotional Ends, Coles typically seeks to highlight products that represent great value for customers and which are

³² See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 18.

³³ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 242.

most likely to sell at high volume. Where suppliers do pay for Promotional Ends or catalogue space, this reflects the supplier seeking additional marketing for a product that Coles would not otherwise market in that way.

In respect of the timing of when promotions are agreed, Coles engages with its suppliers in a collaborative way to plan promotional activity. In all business units other than fresh produce, this typically occurs approximately six months before the beginning of each half year regarding promotions. Planned specials and promotions are then locked in approximately eight weeks in advance to allow time for forecasting, production planning and transport of goods. Promotions in Fresh Produce are generally planned two weeks in advance because of fluctuations in supply and market price. Fresh produce suppliers do not contribute additional funds to promotions but they agree a promotional cost price for the relevant promotional week.

In grocery, Coles' practice is to agree in writing any arrangements for promotional funding with a supplier in advance in a form called a Promotional Advice Form or PAF. There may be isolated instances where a PAF is submitted by a supplier in close proximity to the start date of a promotion commencing. However, this will generally only occur where a revised promotion is negotiated in order to react to market activity (for example, where changes in the competitive environment require revising promotional timing or pricing, which may occur at the request of the supplier) or to address compliance issues (such as where the planned promotion does not comply with Coles' internal business rules). Coles' category managers are required to comply with Coles' Promotions Policy and Procedure. This policy supports compliance with the Grocery Code of Conduct which prohibits any retailer from compelling a supplier to fund a promotion and from cancelling or changing a promotion without providing reasonable notice to the supplier.

4.7 Private label

Coles notes the concerns raised by some suppliers that retailers use private label products to pressure branded suppliers³⁴ or that suppliers face the threat of product deletion where they do not agree to supply private label.³⁵

Coles makes substantial investments in its Own Brand offering in order to provide quality and innovative products to customers at an affordable price. Own Brand products are typically between 10%-40% cheaper for consumers than similar proprietary brands. Offering customers a range of both proprietary and Own Brand products is therefore a key way for Coles to offer value to customers. Investing in its Own Brand offering also positions Coles to better compete with ALDI's offering of predominately internal branded products (which is ALDI's core offering).

Coles Brand products are not introduced into categories to put pressure on proprietary suppliers. They are introduced into a category range because Coles determines (based on research and customer insights) that there is a gap or opportunity and Coles considers that a Coles Brand product would be well placed to address that customer need. For example:

- in 2019, Coles launched **Coles Nature's Kitchen** which provides plant products underpinned by vegan recipes;
- in 2019, Coles launched the **'I'm Free From' ranges** which highlights on the front of the packaging whether they are free from common allergens such as wheat, dairy, eggs and nuts;
- in 2021, Coles launched the **Coles PerForm** range which includes refrigerated and frozen meals that are sports dietitian approved and designed to assist customers to support their health, wellbeing and physical performance. This range has recently expanded to also include a variety of protein powders and protein bars; and
- in 2023, Coles launched **Coles Simply** own-brand products designed to help customers find low cost basic product offers across the store to help them balance their weekly budget such as Coles Simply Classic Tomato Pasta Sauce.

Like proprietary products, the performance of Coles Brand products (e.g., customer sales, margins etc) is kept under ongoing review. Coles Brand products which do not result in significant customer uptake or otherwise do not perform are removed from the range. There are numerous examples where this has occurred. Sometimes customer insights and

³⁴ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 228.

³⁵ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 229.

trends may suggest that there is an opportunity for a Coles Brand product but the product does not ultimately perform to expectation after launch. For example, Coles launched a premium Own brand dog food called Elevate in March 2021, which did not ultimately perform and which was removed from the range. While Coles considered that a high quality pet food formulation would be attractive to customers looking for an alternative to branded products, it ultimately found many consumers continue to prefer branded options for their pet. Similarly, a healthy ready meal range 'Eat Well' launched in 2023 was not successful in its current form and has now been discontinued.

Once Coles identifies a gap or opportunity for private label products, Coles' sourcing team helps to identify potential suppliers and they are typically invited to submit an expression of interest. Whether suppliers wish to supply private label products is a matter for the supplier. Some suppliers only supply private label products to retailers, some suppliers only supply proprietary and some supply a mix of the two.

4.8 Coles supports timely and collaborative resolution of supplier disputes

Coles is committed to working collaboratively with suppliers and ensuring that negotiations are conducted in a fair, reasonable and professional manner.

Coles notes the concern raised by some suppliers in submissions to the Inquiry that they are reluctant to raise any concerns with major supermarket chains.³⁶

There are a range of avenues for suppliers to raise concerns with Coles, including to their primary category manager contact or the BCM or GM in their product category or the Chief of Commercial and Sustainability. Coles was also the first Australian supermarket retailer to implement an independent arbitration process to help resolve commercial disputes with suppliers and has recently appointed former General Counsel of Ford Motor Company of Australia Jenny Linsten as Arbiter under the Grocery Code of Conduct.

While the Arbiter has not received formal complaints under the Code in 2023 – 2024, this does not mean that Coles is not receiving feedback and resolving issues with its supplier base as they arise. Many suppliers raise feedback or any concerns with their category manager or their line manager. Since taking on the role of Coles appointed Arbiter in February 2024, Ms Linsten has taken a range of steps to introduce herself to Coles' supplier base and encourage them to raise queries or concerns with her about their dealings with Coles. This included addressing a fresh supplier forum, participating in a Q&A video distributed to all Coles suppliers, holding meetings with industry associations and consultants that represent suppliers and speaking directly with a range of suppliers at industry sponsored conferences, meetings and events.

Coles is committed to strong and timely dispute resolution with suppliers and welcomes discussion about how existing processes can be improved further. Coles encourages suppliers and industry associations to raise any concerns directly with Coles so that it can review and action as appropriate.

5 Competition in Australia's grocery retailing sector has increased and continues to intensify

Australia's grocery sector has a diverse range of players that each bring different competitive strengths. This includes:

- full line supermarket chains like Coles, Woolworths and Metcash network stores (i.e., IGA stores);
- a national discount chain in ALDI;
- a growing club retailer in Costco;
- a revitalised independent segment;
- a vibrant fresh food specialist network (fruit and vegetable, butchers, bakeries and delis);

³⁶ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 245.

- fresh food markets;
- large national category specialists, such as Bunnings and Chemists Warehouse; and
- fast-growing online players including Amazon and Catch.

Customers' ability and increasing propensity to shop across a mix of these retailers imposes a significant competitive constraint on supermarkets such as Coles who must offer a strong value proposition across the board - through price, range, quality, service, location and convenience – in order to attract and retain customers.

Coles' submission to the Issues Paper detailed the substantial investments in supermarket supply chains, store operations and customer proposition which have occurred since the ACCC's last review of the sector in 2008. That detail is not repeated here. Instead, Coles identifies key areas of the ACCC's current analysis which Coles considers require more detailed consideration in the ACCC's final report to ensure a robust assessment of competitive dynamics in this important sector.

5.1 Cross shopping imposes a significant constraint on supermarkets

While the Terms of Reference are focused on markets for the supply of groceries, Coles notes that the ACCC proposes to focus on supermarkets rather than grocery retailing more generally. This approach is taken on the basis that:

- 96% of respondents to the ACCC's survey indicated that their 'main grocery store' is a supermarket;³⁷ and
- ABS data which suggests that supermarkets account for approximately 85% of consumer spend on groceries.³⁸ Coles notes that the ABS data relied upon includes groceries acquired from supermarkets but *excludes* groceries acquired from other retailers, including online marketplaces and category specialists.

Coles considers that this reflects a narrow approach and Coles supports a robust consideration of grocery retailing more generally.

A broader focus on grocery retailing (rather than supermarket retailing) is also consistent with the ACCC's approach in 2008 where the ACCC considered the veracity of claims at that time that the major supermarkets accounted for 80% of retail sales. The ACCC ultimately concluded that the major supermarket chains accounted for between 55% and 60% of consumer expenditure on grocery items based on share of national take-home food and grocery sales and found that *'to say that the [major supermarket chains] enjoy an 80 per cent share of grocery sales exaggerates the position of the retailers'*. The report went on to consider in detail the major supermarket chains' share of sales by individual product categories, making the following findings:

- *"it is ...clear on closer analysis that the [Major Supermarket Chains]' share of the grocery dollar varies dramatically depending on the food category being examined. Specialty stores sales are substantial in the fresh product categories and therefore need to be considered in any analysis of whether there are competition problems at the retail level";³⁹*
- *"packaged groceries is the category most heavily dominated by the major supermarket chains... a figure of approximately 70% seems a reasonable assessment";⁴⁰*

³⁷ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 138.

³⁸ See ACCC, *Supermarkets Inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 137.

³⁹ See ACCC, *Report of the ACCC Inquiry into the competitiveness of retail prices for standard groceries*, July 2008, <<https://www.accc.gov.au/system/files/Grocery%20inquiry%20report%20-%20July%202008.pdf>>, page 49.

⁴⁰ See ACCC, *Report of the ACCC Inquiry into the competitiveness of retail prices for standard groceries*, July 2008, <<https://www.accc.gov.au/system/files/Grocery%20inquiry%20report%20-%20July%202008.pdf>>, page 51.

- "no more than 50 per cent of fresh fruit and vegetables are sold through the [major supermarket chains]";⁴¹ and
- "approximately 50 per cent of fresh meat is sold through the [major supermarket chains]".⁴²

Coles submits that a similar analytical framework to that adopted by the ACCC in 2008, namely, considering supermarket share of 'grocery dollar', is also appropriate in the current Inquiry. It is notable in particular that at the time of the 2008 Inquiry, in contrast to fresh produce, meat and bakery, there were limited other avenues for customers to purchase packaged groceries and the ACCC found that the major supermarket chains had the highest share of sales in this area. Importantly, the position in respect of packaged groceries has changed significantly since 2008 as customers can now purchase packaged groceries through numerous other channels including from online retailers such as Amazon and Catch, from discount shops such as the Reject Shop and from category specialists such as Bunnings and Chemist Warehouse. None of this is to suggest that a customer can purchase all of their grocery requirements from these channels. However, as the ACCC previously did in 2008, it is important to acknowledge the ability and propensity of customers to split their grocery spend across both supermarket and non-supermarket grocery retailers. This is because the cumulative effect of the customer's ability to split their basket imposes a significant constraint on supermarket retailers such as Coles.

The ACCC's Interim Report acknowledges that most consumers visit multiple stores during a typical week to do their grocery shopping.⁴³ The ACCC's Interim Report also suggests that other grocery retailers may impose a degree of competitive constraint on supermarkets where their offerings overlap.⁴⁴ Coles agrees that the risk of customers splitting their baskets across supermarket retailers is a key competitive dynamic in the modern grocery environment that must be examined by the ACCC, particularly because it is facilitated by the colocation of supermarkets with specialty and category retailers as well as the increasing convenience of online shopping. However, there is no logical reason to restrict an analysis of basket splitting to supermarket retailers only. The ability and increasing propensity of customers to disaggregate their baskets across supermarkets, online retailers, category specialists and specialty retailers such as greengrocers and butchers must be examined to ensure a fulsome picture of the competitive landscape.

Importantly, Coles submits that the ability of customers to disaggregate their spend across retailers imposes competitive tension not only in areas of product overlap. Rather, to remain a 'one stop shop' and win as much of the customer's basket as possible, supermarkets must offer customers a compelling proposition across the board, through value, range, location, convenience and service. Supermarkets are strongly incentivised to do so as they make higher and lower margins across different product categories and look to balance their return across the customer's shopping trip as a whole. If supermarkets lose a substantial proportion of these sales through cross shopping behaviour, the economics of supermarket retailing are undermined.

As demonstrated at Figure 5 of Coles' submission to the Issues Paper, 62% of Australians surveyed for Coles shop with 2-3 different supermarket brands each month and 19% shop with 4 or more different brands each month. In comparison to other countries, Australians cross-shop more than customers in New Zealand (2.2), the United States (2.3), Canada (2.5) and the United Kingdom (2.7).

⁴¹ See ACCC, *Report of the ACCC Inquiry into the competitiveness of retail prices for standard groceries*, July 2008, <<https://www.accc.gov.au/system/files/Grocery%20inquiry%20report%20-%20July%202008.pdf>>, page 53.

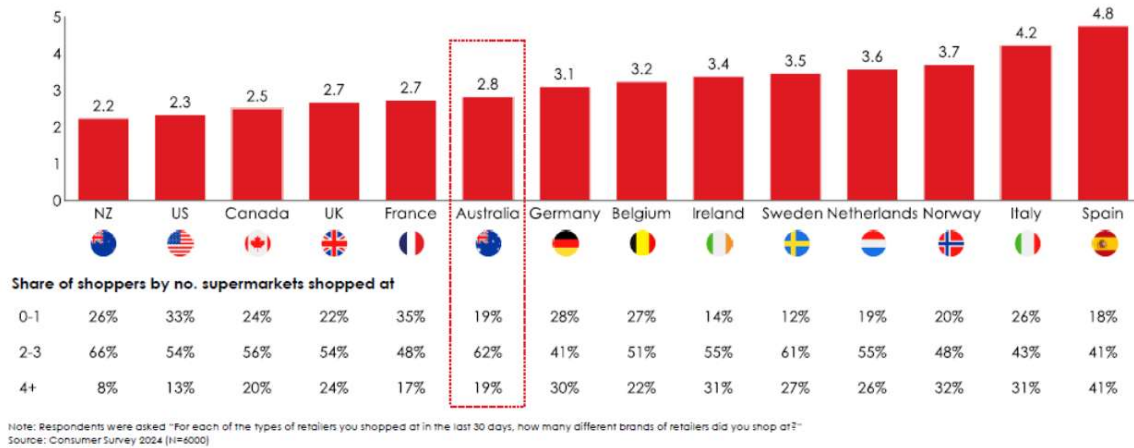
⁴² See ACCC, *Report of the ACCC Inquiry into the competitiveness of retail prices for standard groceries*, July 2008, <<https://www.accc.gov.au/system/files/Grocery%20inquiry%20report%20-%20July%202008.pdf>>, page 54.

⁴³ See ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 153.

⁴⁴ See ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 153.

Figure 5: Cross-shopping between supermarkets across jurisdictions

Q: How many different brands of supermarkets did you shop at in the last 30 days?
 (% of consumers by # of supermarkets shopped at per month)



Note: Respondents were asked "For each of the types of retailers you shopped at in the last 30 days, how many different brands of retailers did you shop at?"
 Source: Consumer Survey 2024 (N=6000)

5.2 Price is important, however all aspects of competition must be considered

The Interim Report notes that customers consider a range of factors when deciding where to purchase groceries. This includes convenience, value, range and quality.⁴⁵ While the Interim Report acknowledges these aspects of competition, the ACCC's analysis then focuses predominantly on price and price competition.⁴⁶ It is worth noting that the UK CMA has long used a Price, Quality, Range and Service (PQRS) methodology to measure competition. In some markets it has added Innovation to this list.⁴⁷

Coles agrees that price is a very important dimension to competition and it is appropriate that the Inquiry places particular focus on price, especially during the current cost of living crisis. However, price is one of a number of aspects of competition in grocery retailing. A comprehensive review of Australia's grocery sector requires due consideration be given to material non-price elements of competition such as product quality, product range, service, location and online capabilities. While these factors are noted in the Interim Report, there is limited analysis of how retailers compete on these dimensions. Coles supports a comprehensive review of these other aspects of competition.

Coles' own experience pre-demerger in 2018 was that a focus on price competition over and above other drivers of value resulted in an impact on its competitive position. Reduced investment in Coles' fresh food offering and store renewal program together with range reductions alienated many customers, resulting in declines in Coles' market share. Since demerger, Coles' corporate strategy has been to focus on price competition but also on other drivers of value. Coles' subsequent investments in price competitiveness, store refurbishment, store format, own brand product development, range (especially in health, convenience) and immediacy and home delivery reflect very vigorous competition, both in response to its competitors but also to changing customer needs.

⁴⁵ ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 152.

⁴⁶ See ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, section 7.2.1.

⁴⁷ CMA, *Retail Mergers Commentary*, <<https://assets.publishing.service.gov.uk/media/5a81e8e840f0b62302699d23/retail-mergers-commentary.pdf>>, page 5.

(a) Product quality

Product quality and innovation is a key component of the customer offer and a significant focus for grocery retail competition. Examples of how Coles has competed strongly in this respect include:

- **Focusing on own brand to compete for cost-conscious consumers:** This includes investment in increasing the quality and variety of private-label products, to position them as high-quality affordable alternatives to branded items. This is particularly important to attract cost-conscious customers who are likely to place significant value on ALDI's offering.
- **Commitments to local and ethical sourcing to compete on quality of produce:** This includes the Australia First sourcing policy and ethical sourcing practices which prioritise collaboration with local suppliers for ethically sourced Australian-grown products. For example, Coles offers cage-free eggs, hormone-free beef, and sustainably sourced fish and ensures 100% of fresh meat and 96% of fresh produce sold is grown in Australia. Additionally, since launching its Nurture Fund in 2015, Coles has provided more than \$33 million to small and medium sized farmers and producers to support local innovation projects (including a carbon neutral banana range, systems to divert packaged food waste from landfill and a new farrowing system to improve animal welfare standards in pork production).
- **Adapting dynamically to changing customer trends and preferences:** This includes developing new products to meet customer demand for convenient, sustainable and health-focused meal options. For example, in recent years, Coles has introduced a plant-based range (Nature's Kitchen, 2019), a chilled and ready-to-eat meal range (Coles Kitchen, 2020),⁴⁸ a premium restaurant-quality ready meals range (Coles Finest, 2020), a sport dietitian approved frozen meal range (Coles PerForm, 2021) and an organics range. Additionally, Coles has sought to make customers' preferences more accessible, for example, the 'Health in Every Aisle' initiative (2022) moved items like gluten-free pasta from the health food aisle into their respective product categories.

Coles' experience pre-demerger demonstrates that customers strongly value quality and innovation and will switch away from retailers where an offering does not meet their needs. Prior to Coles' demerger from Wesfarmers, it implemented some range rationalisation to reduce its costs and become more efficient. However, a decline in sales and strong customer feedback revealed that Coles' ranging changes had gone too far and Coles lost market share as a result. Now more than ever, Coles puts customers at the centre of product offering decisions, and when seeking to optimise its ranging, uses customer and data insights to ensure that it is taking a customer centric approach.

(b) Location and store networks

The time and investment required to expand in Australia is a feature of the Australian grocery retail landscape owing to Australia's geography and relatively low population density. However, location and convenience are key aspects of retail competition and a review of the investments by competitors since 2008 demonstrates vigorous competition between grocery retailers as they build or enhance their store networks.

Importantly, ALDI has increased its store count from 166 stores in 2008 to 592 stores currently while Costco has built 15 stores across Australia. The Interim Report notes that Metcash / IGA's net store count has declined over time but there has been an important uptick since 2015, with renewal and investment in the Metcash business leading to record store openings in FY23 and FY24. Other independents, such as Drakes (60 stores) and Harris Farm (27 stores), have also grown substantially and flagged their plans to expand further.

In contrast, both Coles' and Woolworths' expansion of their networks over time has been relatively modest, with Coles increasing its fleet by only 89 stores since 2008. A key focus for Coles has been on optimising and improving its existing network ie to ensure it has the "right store in the right location". Competition for retail sites is therefore another key aspect of competition between supermarkets. Importantly, while competition for retail sites reflects a further dimension of supermarket competition, Coles does not consider competition for retail sites to be a barrier to entry or expansion. Given their similar store formats, Coles most commonly competes head-to-head with Woolworths in respect of both leasehold and freehold sites (including in respect of acquisitions of shopping centres). In addition, many new stores are opened by Coles or Woolworths in undeveloped urban regions or growth corridors where store development occurs in anticipation of population reaching sustainable levels. Coles does not typically see ALDI, IGA or other independents enter these locations until population is well established, again, meaning that Coles is typically competing head-to-head with

⁴⁸ Coles notes that the Coles Kitchen range was relaunched in 2020.

Woolworths in relation to these greenfields opportunities. By virtue of their scale, it is typically either Coles or Woolworths that brings new supermarkets to emerging urban communities across Australia.

As noted in Coles' submission to the Issues Paper, supermarkets have also sought to respond to increasing competition and changes in consumer preferences with changes to store format that maximise convenience for customers. For example, Coles offers convenience food ranges in a dedicated front of store convenience space that allows customers to quickly pick up 'food for now' and 'food for later'. Woolworths, ALDI and IGA stores feature a similar designated area closely to the front of the store and/or the registers which allows customers to quickly purchase a range of ready-to-eat or easy-to-cook meals.

(c) Online

While the Interim Report acknowledges that some customers undertake grocery shopping online, the focus is on bricks and mortar grocery retailing, with the Interim Report observing that only 15% of respondents to its consumer survey currently buy most of their groceries online.⁴⁹ The Interim Report also suggests that competition from Amazon may be limited to a relatively small range of products.⁵⁰

Coles is surprised that competition in online grocery retailing receives such limited consideration in the Interim Report. Coles considers that online retailing presents a significant and growing threat to the traditional grocery sector – particularly given the ability of customers to split their baskets across retailers with convenient online purchases as discussed in section 5.1 above.

Although the ACCC's consumer survey has provided a number of useful insights, Coles considers that there appears to be an over reliance on the current shopping preferences of a relatively small subset of customers regarding the competitive threat of online retailers in particular. It disregards evidence from the supply side (i.e., Coles' internal documents which demonstrate that Coles' business strategies are responding to the threat of Amazon and other non-supermarket retailers) and also the *potential* competition posed by these businesses even if many customers are currently sourcing groceries from bricks and mortar supermarkets.

Putting the threat of online market places such as Amazon and Catch to one side, due consideration of online is also important because it reflects a significant domain of competition between existing supermarket retailers.

As outlined in Coles' response to the Issues Paper, Coles has experienced significant increases in uptake of delivery and click and collect services since the COVID-19 pandemic, a trend which has largely remained as time-poor and convenience-driven Australians are increasingly willing to move their grocery shop online. Coles Online sales increased from 4% of overall sales in FY20 to 5.8% in FY21, to 8% in FY22 and up to 9.1% in the first half of FY24. In August 2024, Coles announced that its e-commerce sales had increased 30% since the year prior, reaching \$3.7 billion in the 53 weeks to June 30, up from \$2.8 billion in FY23.⁵¹

To meet this surge in demand and compete with other grocery retailers' online offerings, Coles has had to respond with significant investments in online. This includes launching same-day home delivery at over 480 stores and Click & Collect Rapid at over 600 stores in 2023. In addition, to facilitate efficient, accurate and on-time delivery of the home delivery orders, Coles has recently spent more than \$400 million in capital expenditure on two automated Customer Fulfilment Centres in Queensland and NSW that use robotics to pick and pack orders. Alongside improvements in delivery logistics, Coles has also focused on refining its digital platform, upgrading its app to be fully e-commerce enabled and consolidating its website into a single shopping experience. New features include an in-store mode for the app, used by 55% of app users, the ability to opt-in for substitutions at checkout, advanced filtering options for dietary preferences, and Flybuys integration.

⁴⁹ ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 154.

⁵⁰ ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 158.

⁵¹ Canberra City News, *Coles looking to grow already strong online sales*, 27 August 2024, <<https://citynews.com.au/2024/coles-reports-30-jump-in-online-supermarket-sales/>>.

Reflecting a competitive environment, Coles' investments in online have prompted or responded to similar investments from other supermarkets. For example, Woolworths now offers an extensive delivery network with same-day options with a sophisticated app offering⁵², while Metcash and independent stores (including IGA, Harris Farm and Drakes) also offer online delivery and click and collect options.⁵³ The growth in "Q-commerce", where third party delivery platforms facilitate 'immediate' grocery ordering (for example, through UberEats and DoorDash) has allowed grocery retailers of all sizes and scale to offer a competitive delivery service.

5.3 Competition in grocery retailing is intensifying

The Interim Report does not express a view on the level of competition in grocery retailing but it suggests that Australia's supermarkets sector is highly concentrated.⁵⁴

When regard is had to Australia's geography and relative population size, Coles does not consider the current number of national supermarket chains (Coles, Woolworths, ALDI and IGA) to be surprising. It takes time and cost to build a national network, and Coles' and Woolworths' own networks have taken many years to establish. However, ALDI's rapid growth in Australia demonstrates that new supermarket chains can enter and expand over time and Coles considers that the Australian grocery sector remains an attractive market for overseas grocery chains as well as expansion by local players.

Coles submits that competition in Australia's grocery landscape is strong and intensifying over time, particularly as differentiated retail formats open up and expand in the Australian landscape. Coles currently faces competition from two national full line supermarkets (Woolworths and IGA), a national hard discount chain (ALDI), a growing club retailer (Costco), a vibrant independent and specialist network and fresh food markets and fast-growing online players including Amazon and Catch. Whilst IGA store numbers have declined since 2008, it is important to note that renewal and investment in the Metcash business from around 2015 has seen a reinvigorated IGA store network and record new store openings in FY23 and FY24.

While each competitor brings their own competitive strengths, Coles notes that the ACCC is particularly focused on the level of competition between Coles and Woolworths given their similar formats and breadth of store network. As anyone who has worked at a major supermarket chain can attest, the competitive rivalry between Coles and Woolworths on all fronts is fiercely intense. For many years, Coles has targeted lower prices than Woolworths at an overall supermarket level. Any similarity in pricing reflects vigorous competition as Woolworths and Coles seek to match or better one another's price reductions. Moreover, a review of competition since the ACCC's 2008 Inquiry reveals not only vigorous day to day competition, but very substantial capital investments in value, store renewal and supply chain modernisation over the years as each major supermarket chain seeks to reset and refresh its strategy and lead sales growth. Examples include the dramatic turn around of the Coles business in the years following Wesfarmers' acquisition in 2007, Woolworths' strategy reset in 2015 / 2016 which saw it overtake Coles' sales growth through a \$1 billion investment in price reductions, Metcash's implementation of its major transformation plan since 2015 and Coles' partnerships with Witron to develop three automated DCs in Brisbane, Sydney and Melbourne at a cost of \$1.88 billion. These major investments are not discussed in the Interim Report but they are an important feature of how competition has occurred in grocery retailing, with Coles, Woolworths and other supermarket chains expanding their shares or falling behind depending on their investments in the customer offer, their store network and in supply chain modernisation.

⁵² Woolworths, *2023 Annual Report*, <<https://www.woolworthsgroup.com.au/content/dam/wwg/investors/reports/2023/f23-full-year/Woolworths%20Group%202023%20Annual%20Report.pdf>>, page 9; MILKRUN, <<https://www.milkrun.com/au/>>, page 3.

⁵³ IGA, *IGA Shop Online*, <<https://www.iga.com.au/shop-online/>>, viewed on 6 November 2024; Metcash, *2023 Annual Report*, <<https://www.metcash.com/wp-content/uploads/2024/08/2024-Annual-Report.pdf>>, pages 14, 24; Harris Farm Markets, *Delivery Info*, <<https://www.harrisfarm.com.au/pages/delivery>>; Drakes, *Online Shopping*, <<https://online.drakes.com.au/>>.

⁵⁴ See ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 145.

Coles agrees with the ACCC's finding that ALDI is an important source of competitive constraint on Coles and Woolworths⁵⁵ but disagrees that ALDI provides only a partial 'price constraint'. A review of Coles' internal documents which have been produced to the ACCC demonstrates a very high degree of focus on ALDI's pricing and competitive behaviour. While ALDI's range is more limited, it has grown over time (especially in fresh produce and branded products), and areas of overlap generally include the highest volume staples that form a core component of a customer's shopping basket. In addition, while ALDI's network is not as extensive as Coles and Woolworths, Coles' pricing is generally consistent nationally, which means that the pricing constraint imposed by ALDI is not limited to those states or locations where it currently has stores.

5.4 Cost management and efficient capex

As discussed in further detail in section 6 below, the Interim Report focusses mainly on financial metrics which exclude costs other than COGS entirely (i.e., shelf margin) or exclude key cost components (i.e., EBIT, which excludes interest paid on debt, especially for major capital expenditure). As discussed in section 6 of this submission, while COGS is a key operational cost, other significant costs include labour, rent and energy.

Because of the low margins earned relative to many other industries, small increases in costs for a national supermarket operator will have significant impacts on profitability. Because of this, major supermarkets devote substantial efforts to minimise increases in their costs. A major part of the Coles Corporate Plan and the focus of the Executive Team is cost control. From 2018 to 2022, Coles saved over \$1 billion in its Smarter Selling cost-out program, with a similar target for the current Simplify & Save to Invest program. As the name of this program suggests, Coles relies on the savings generated through cost savings to reinvest in its business, including product prices.

Although cost management is therefore a very important feature of competition in the industry, the Interim Report is silent on this issue. For example, in the last 4 years, Coles has invested almost \$2 billion into major supply chain automation facilities, through automated DCs, and customer fulfilment centres. This simultaneous investment in automation of the distribution of products to stores, and deliveries direct to customers, is almost without precedent in the world. It has placed Coles in a relatively unique position in the global supermarket industry. The aim of this investment is to give Coles a competitive advantage in terms of lower distribution costs, and in the case of the customer fulfilment centres, fresher produce and higher correct order fulfilment rates than store-based models. These efficiencies are needed to offset the significant drag on profitability that will arise through annual increases in costs that Coles has limited control over, such as rent, energy and labour rates. If Coles did not face substantial competition, it would have had no incentive to make the significant capital expenditure and incur the associated interest costs. Coles would also have had no incentive to take on the substantial risks involved in greenfield investments in new technology of this scale.

Coles believes that efficiency programs by the major supermarkets are one of the reasons why Australian food CPI was lower than overall Australian CPI, and lower than global inflation. Coles considers that a comprehensive review of competitive dynamics must consider competition between supermarkets to reduce their costs.

6 Supermarket profitability

The Interim Report notes that elevated margins and profitability can potentially indicate the exercise of market power (though not necessarily amount to a contravention of the law). As such, the ACCC has indicated that it is considering profitability of supermarkets, as this may provide insights into the level of competition in the market.⁵⁶

While the ACCC acknowledges that there are various profitability metrics and 'no "one size fits all" metric that will be best for all entities, circumstances and purposes', the analysis in the Interim Report focuses on:

⁵⁵ See ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 166.

⁵⁶ ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 191.

- Coles' and Woolworths' EBIT margins over time (which are said to have increased)⁵⁷;
- Coles' and Woolworths' EBIT margins as compared to a selection of international peers (which are said to be more profitable than at least some overseas peers)⁵⁸; and
- Coles' and Woolworths' return on capital (which is acknowledged to be broadly in line with international peers)⁵⁹.

Whilst the grocery sector may historically have been considered a lower risk sector, the ACCC's assertion that supermarkets are 'relatively low risk businesses' is at odds with the significant investments being undertaken by grocery retailers (including Coles).⁶⁰ The shift to online in particular means that grocery retailers are increasingly taking higher risk investments, such as those outlined above at section 5. The construction of the automated DCs and customer fulfilment centres by Coles carried significant risk, given the technology had never been deployed in Australia before and involved major construction projects that all occurred over the COVID period. Some analysts commented after the commissioning of those projects that they had been too conservative about Coles' ability to deliver the projects (i.e., that the risks might mean Coles failed to complete them). Many of these investments reflect substantial efforts to minimise annual cost increases (including the Smarter Selling and Simply & Save To Invest programs).

Risky investments of this type are consistent with the presence of significant competitive constraints on Coles. Absent competition, Coles would not have any incentive to outlay significant sunk costs but must do so to reduce costs over the long term, satisfy customers' needs and avoid losing sales to rivals in the future. Due to these recent investments, Coles' (and Woolworth's) recent annual capital expenditures, as a proportion of revenue, are among the highest relative to the international peers cited by the ACCC in its Interim Report.

6.1 NPAT margin is a more appropriate profit measure and has remained stable

While EBIT is an important measure of profitability for various purposes (including investor reporting), Coles considers NPAT margin to be a more appropriate profitability metric for the purpose of providing insights into the level of competition in the grocery sector. This is because NPAT is an absolute profit calculation which considers all income and costs associated with running a supermarket business. NPAT is also the basis for dividend payments and CEO remuneration is linked to both Group EBIT and Group NPAT.

Importantly, Coles Group's NPAT margin has remained relatively flat across the last five years, and since 2019, has decreased from 2.80% to 2.58% (as shown in figure 2 below). Put another way, for every \$100 in operating revenue, Coles earned NPAT of \$2.80 in 2019 and \$2.57 in 2024.

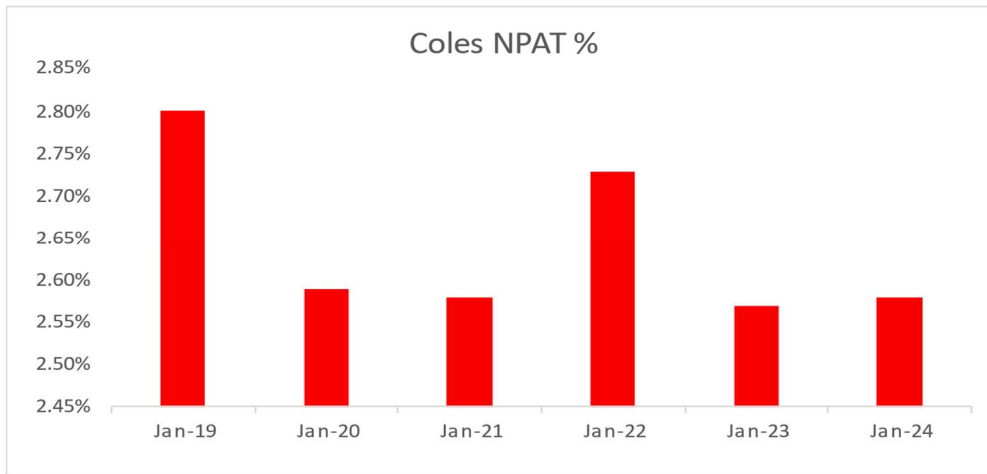
⁵⁷ ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 194.

⁵⁸ ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 197.

⁵⁹ ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 198.

⁶⁰ ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 192.

Figure 2: Coles Group NPAT Margins, 2019-2024



While Coles Group's NPAT margin has remained relatively flat over the last 5 years, it is important to note that Coles in fact experienced significant increases in costs over this period. As outlined in Coles' submission to the ACCC's Statement of Issues, Coles Group's costs increased as follows over the period FY19 to FY24, including:

- Coles' employee costs increasing by almost \$600 million per annum, driven by wage increases (as well as additional team members);
- Payroll tax payments increasing by 19% from \$253 million in 2020 to \$301 million in 2023, due to increased tax rates and higher wages; and
- Increases in energy, logistics and packaging (among other costs), which drove a \$1.4 billion increase in Coles' operating costs.

However, while Coles' costs increased significantly, substantial resources were also devoted to cost reduction measures. For example, from 2018 to 2022, Coles saved over \$1 billion in its Smarter Selling cost-out program, with a similar target for the current Simplify & Save To Invest program.

6.2 Domestic EBIT trends provide limited insights due to accounting standards changing

Notwithstanding that Coles considers NPAT to be the most appropriate measure of profitability for the ACCC's purposes, Coles respectfully submits that the EBIT analysis in the Interim Report – and particularly the conclusion drawn that EBIT margins for each of Coles and Woolworths have increased over the five year period from FY18 to FY23⁶¹ – is incorrect.

This is because the measurement of EBIT margins over the period analysed by the ACCC is affected by changes to accounting standards that were adopted in Australia in 2019-20, and these changes mostly explain the increases in EBIT margins noted in the Interim Report.

The adoption of Australian Accounting Standards Board 16 (AASB 16) in 2019 changed the treatment of leases in calculating EBIT.⁶² The changes have resulted in measures of EBIT (and EBIT margin) increasing compared to pre-AASB

⁶¹ ACCC, *Supermarkets inquiry Interim Report*, August 2024, <<https://www.accc.gov.au/about-us/publications/serial-publications/supermarkets-inquiry-2024-25-reports/supermarkets-inquiry-august-2024-interim-report>>, page 194.

⁶² These changes were adopted into Australian accounting standards by means of AASB 16. AASB 16 ensures that financial statements faithfully represent lease transactions. Prior to AASB 16, leases were treated as expenses with no implications for the balance sheet. For a lessee, AASB 16 requires recognition of (a) a right-of-use asset, representing its right to use the leased asset; and (b) a lease liability, representing its obligations to make lease payments. Consistent with this treatment, the lessee must depreciate the right-of-use asset over the life of the lease and recognise lease payments as being comprised of separate interest and principal payments on the lease liability.

16, because pre-AASB 16 reporting deducts the full lease expense from the calculation of EBIT whereas post-AASB 16 reporting deducts only depreciation of the right-of-use asset from the calculation of EBIT (and not interest on the lease liability).

Coles leases many of the premises on which its supermarkets are located. It follows that a comparison of EBIT margins following the application of AASB 16 cannot be compared directly to EBIT margins before the application of AASB 16, as the ACCC does in its Interim Report, without considering the effect of these changes.

Coles' 2020 annual report documents the effect of the introduction of AASB 16 on its EBIT. It shows that of the \$1,762 million EBIT reported for the group in FY20, \$375 million is due to changes in accounting standards, rather than changes in underlying profit.⁶³ This change is associated with an EBIT margin that is 1.0 percentage point higher, as a proportion of total revenues in FY20 of \$37,784 million, than would have been reported under the accounting standards that applied before FY20.

Coles' group EBIT margin increased from 3.8% in 2018-19 to 4.7% in FY20. It follows that Coles' reported group EBIT margin would have decreased to 3.7%, but for the effect of AASB 16.

Over the period analysed by the ACCC in the Interim Report, from FY18 to FY23, Coles' EBIT margins for its supermarkets segment increased by 0.9 percentage points, from 3.9% to 4.8%. This overall increase is less than the effect of AASB 16 on EBIT margin for the group, which indicates that the profitability margins of Coles' supermarket segment is unlikely to have changed materially over this period.

Coles notes that the slight increase in EBIT margin for Coles' Supermarkets segment in FY24 can in part be explained by the unique nature of FY24 being 53 weeks. There are a range of costs within Coles' business that are accounted for on a monthly rather than daily basis. This means that from an accounting perspective, in a 53 week year Coles records an additional week of sales as well as incremental direct trading costs, but not an increase in all its cost line items. This results in significant operating leverage being recorded for that 53rd week. Examples of costs that Coles accounts for on a monthly basis, and therefore do not increase, are Store Support Centre salaries, property services and lease related expenses that flow through depreciation and amortisation and financing costs.

6.3 Retail price increases have been driven predominately by supplier cost price increases

The factors that have driven increased operating costs for Coles (including wage increases, increased tax rates and increased energy, logistics and packaging costs) have also impacted suppliers. Coles has previously provided evidence to the ACCC that cost price increase requests from suppliers more than doubled from FY21 to FY22 (from 1,101 in H2 FY21 to 2,219 in H2 FY22) with key reasons provided by suppliers to support their requests being cost increases they had experienced in relation to packaging, freight, utilities, wheat, labour and international shipping. These increases in costs were highlighted by numerous submissions to the Inquiry.⁶⁴

Coles' relatively stable NPAT margin is consistent with increases in retail prices generally rising commensurate with (rather than over and above) these supplier cost price increases. This is also in line with ABS statistics which support a finding that movements in the consumer price index (CPI) for 'food and non-alcoholic beverages'⁶⁵ have generally been consistent

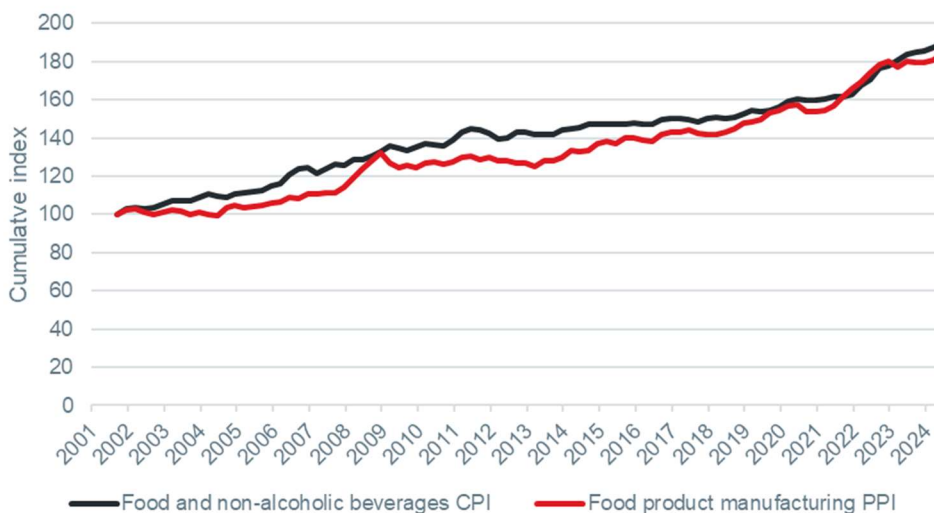
⁶³ Coles, *Annual Report 2024*, August 2024, <https://www.colesgroup.com.au/FormBuilder/_Resource/_module/ir5sKeTxxEOnzdhd00hWJw/file/Annual_Report_2024_Online_Tab.pdf>, page 38.

⁶⁴ See, eg, Australian Fresh Produce Alliance, *Response to the ACCC's Issues Paper*, <<https://www.accc.gov.au/system/files/Australian%20Fresh%20Produce%20Alliance-Public.pdf?ref=0&download=y>> page 2; Australian Meat Industry Council, *Response to the ACCC's Issues Paper*, <<https://www.accc.gov.au/system/files/Australian-Meat-Industry-Council-Public.pdf?ref=0&download=y>> page 8; AUSVEG, *Response to ACCC's Issues Paper*, <https://www.accc.gov.au/system/files/AUSVEG_Redacted.pdf?ref=0&download=y>, page 5.

⁶⁵ Australian Bureau of Statistics, *Consumer price index, Australia*, category number 6401.0, Table 3, 'Food and non-alcoholic beverages', series ID A2325891R.

with changes in the producer price index for 'food product manufacturing'.⁶⁶ This indicates that, across the sector over time, movements in retail prices reflect commensurate movements in supplier prices.

Figure 3: Relative movements in food measures of CPI and PPI, 2001 to 2024



6.4 Coles' profitability is in line with international comparators

As Coles noted in its submission to the Issues Paper, international comparisons of profitability are inherently difficult. However, if the ACCC is to compare the profitability of Australian supermarkets to international peers, it should undertake this comparison on the basis of 'NPAT margin', reflecting the ratio of net profit after tax (NPAT) to revenue. Doing so reveals that Coles' NPAT margins are broadly in line with international peers.

As previously indicated to the ACCC, Coles considers NPAT to be a more useful metric for comparing businesses operating between jurisdictions. This is because NPAT is a measure of profit that takes into account all income and costs associated with running a business. It is defined in international accounting standards and is consistently reported across geographies and periods. By comparison, EBIT excludes key cost components (like interest and taxes) that can vary significantly between jurisdictions. Furthermore, compared to EBIT, NPAT is less affected by differences in accounting standards between jurisdictions, and also less affected by differences in property portfolio (e.g., ownership versus leasing) due to AASB16.

The international peers analysed by the ACCC in its Interim Report operate across countries including the United States, the United Kingdom, Canada and France. The table below sets out a comparison of corporate tax rates and corporate bond yields⁶⁷ between these jurisdictions and Australia.

⁶⁶ Australian Bureau of Statistics, *Producer price indexes, Australia*, category number 6427.0, Table 12, 'Food product manufacturing', series ID A3343827C.

⁶⁷ Measured for the purpose of this comparison as the benchmark yield on five-year BBB rated corporate bonds over the 2023-24 financial year.

Table 1: Corporate tax rate and bond yield comparisons

Jurisdiction	Corporate tax rate	Corporate bond yield
United States	21%	5.47%
United Kingdom	25%	5.57%
Canada	27%	5.14%
France	25%	3.73%
Australia	30%	5.71%

Note: the calculation of the Canada corporate tax rate assumes 15% federal tax plus the most common provincial/territorial rate of 12%.

The table above shows that Australia has higher corporate tax rates and bond yields than the countries with which the ACCC draws EBIT comparisons in its Interim Report. These differences can have a material impact on EBIT comparisons. For example, a firm with similar characteristics to Coles, with revenue of \$40 billion, total assets of \$20 billion and gearing of 25%, would require different levels of EBIT margin in different jurisdictions to deliver a NPAT margin of 2.5%.

The calculation of these different EBIT margins, given differences in corporate tax rates and bond yields, is set out in the table below. The table demonstrates that, for a firm with characteristics similar to Coles' and using bond yield data from 2023-24, EBIT margins would need to be higher in Australia than in other jurisdictions, by as much as 0.38%, to account for higher corporate tax rates and higher interest costs. These differences would likely be higher if historical differences in corporate bond yields, reflected in interest costs paid on current debt portfolios, were factored into the calculation.

Table 2: Required EBIT margin to deliver 2.5% NPAT margin

Jurisdiction	NPAT (\$ million)	Tax (\$ million)	Interest (\$ million)	EBIT (\$ million)	EBIT margin
United States	1,000	266	273	1,539	3.85%
United Kingdom	1,000	333	279	1,612	4.03%
Canada	1,000	370	257	1,627	4.07%
France	1,000	333	186	1,520	3.80%
Australia	1,000	429	285	1,714	4.28%

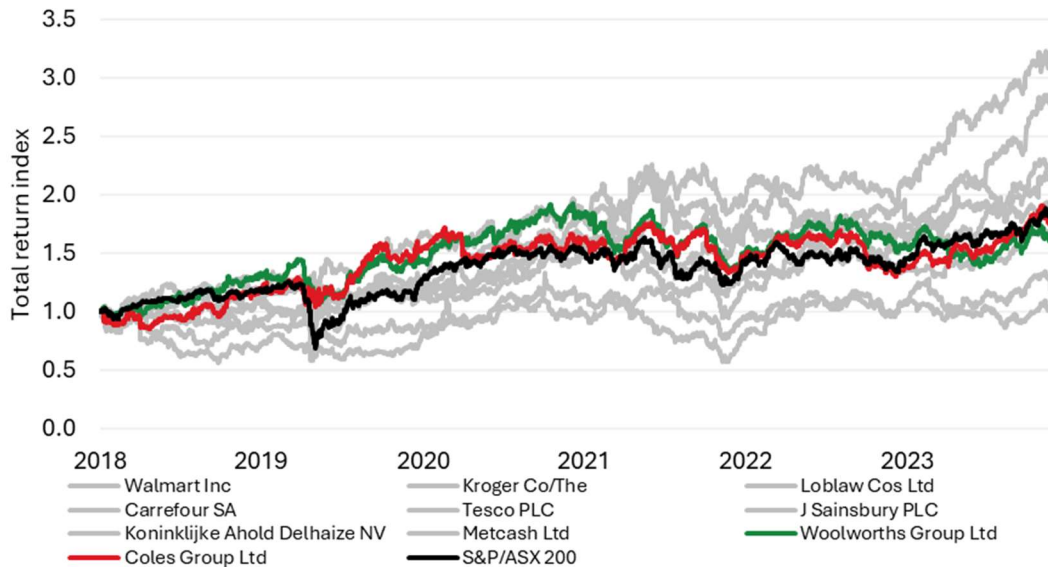
Another method by which the competitiveness of the groceries sector might be assessed is to examine total shareholder return over a period of time. If the groceries sector was becoming less competitive over time, this may be expected to be reflected through high returns to shareholders over time, relative to a benchmark share index or to comparator firms.

The figure below shows the total shareholder return since Coles' 21 November 2018 re-listing date for Coles, Woolworths, and each of the ACCC's comparators, as against the return on the ASX 200.⁶⁸ The chart shows that returns for shareholders for Coles and Woolworths over this period have been in line with the overall Australian market and are broadly typical of comparison firms. The ACCC's comparison firms include examples with higher returns (such as Loblaw)

⁶⁸ Returns are calculated in local currencies and no currency conversions are undertaken.

and lower returns (such as Tesco and Carrefour). These outcomes do not support any conclusion that there is a declining degree of competitiveness in the Australian groceries sector.

Figure 4: Total shareholder returns since 21 November 2018



6.5 Coles' profitability is also in line with domestic comparators

Profitability comparisons between Australian supermarkets and other Australian retail businesses on the basis of EBIT are less problematic than international comparisons given that they share a common tax and bond yields (although examining trends over a period that combines pre and post AASB 16 must be treated with caution).

The charts below show EBIT margins, NPAT margins and ROC for Coles and Woolworths as compared to a sample of listed retailers comprising Wesfarmers, JB Hi Fi, Harvey Norman, Premier Investments, Lovisa Holdings, Super Retail and the Reject Shop. For EBIT margin comparisons, the Officeworks, Bunnings and Kmart segments of Wesfarmers are also included in these comparisons.

These results highlight that, notwithstanding unusual years explained by one-off accounting events,⁶⁹ profitability outcomes for Coles and Woolworths are within the normal range for Australian retailers, typically being the lowest amongst firms in this sample with the exception of the Reject Shop.

⁶⁹ For example, Coles' ROC in 2019-20 is overstated due to the one-off change in accounting treatment of leases. This is because the average of total capital will be understated for Coles in 2019-20 since its capital recorded for 2018-19 excludes the right-of-use value or leases, resulting in an ROC that is overstated.

Figure 5: EBIT margins for Australian retail businesses, 2019-20 to 2023-24

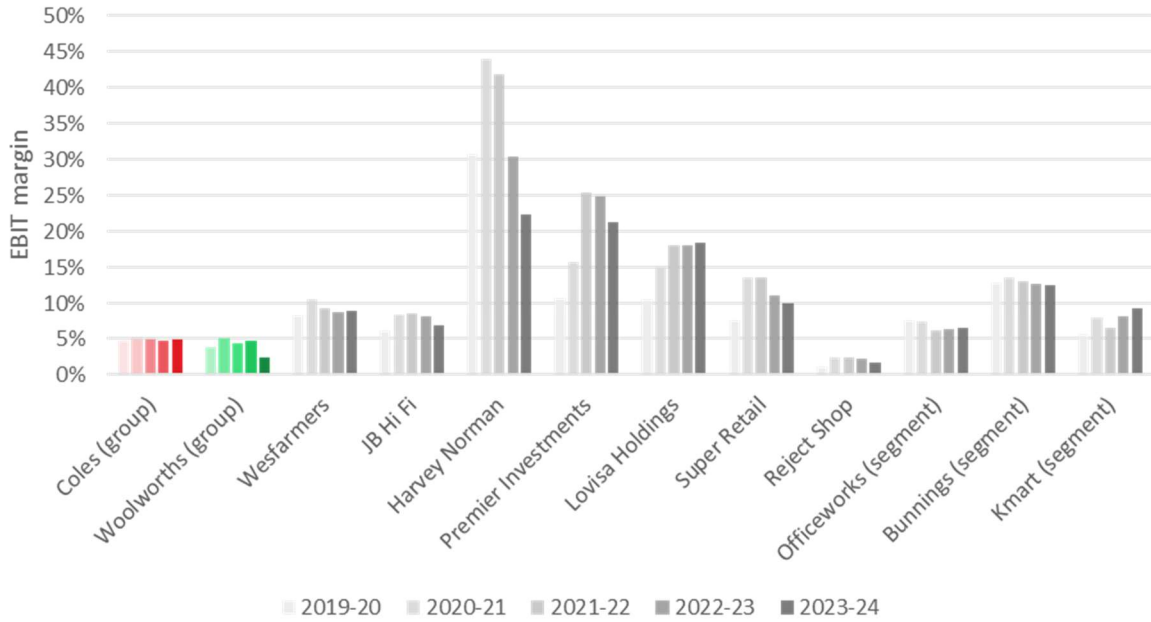


Figure 6: NPAT margins for Australian retail businesses, 2019-20 to 2023-24

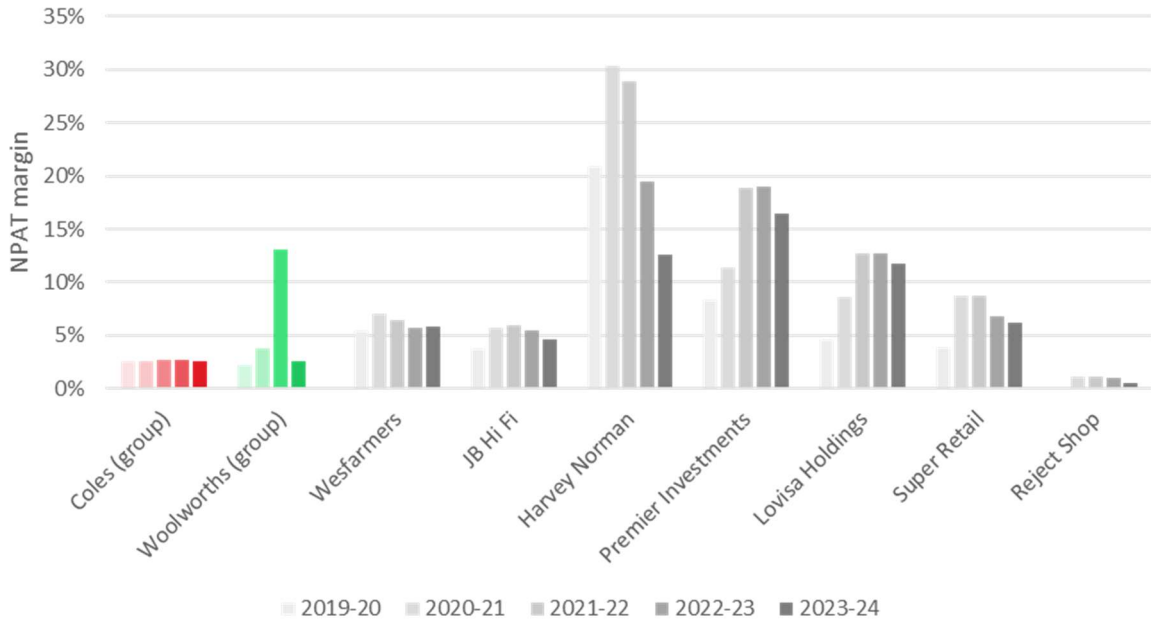
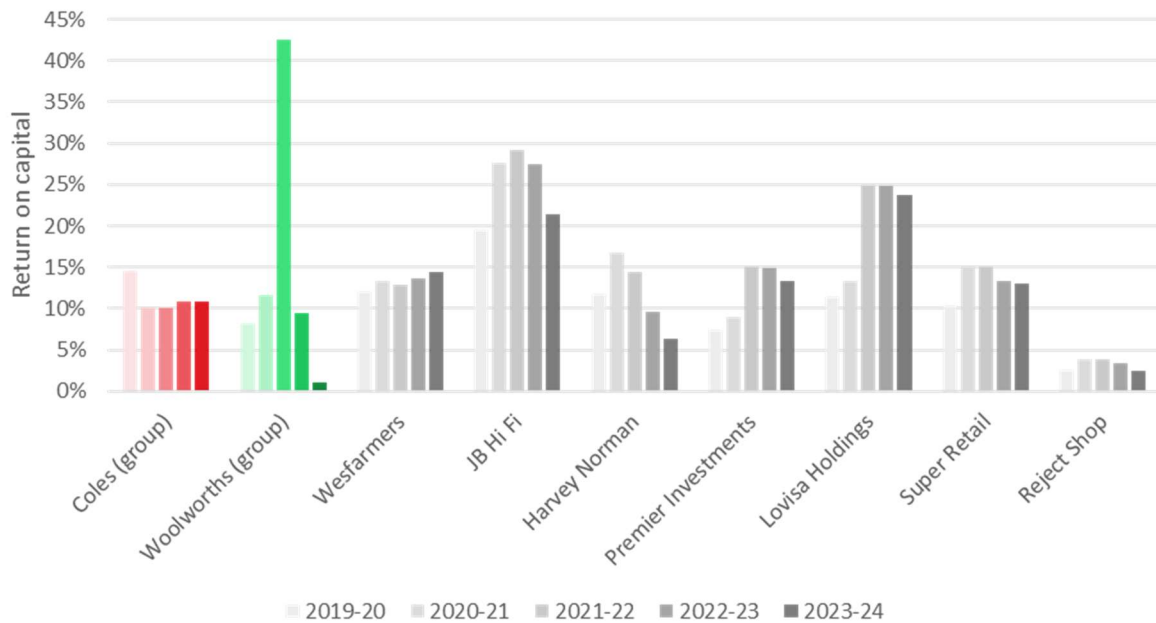


Figure 7: ROC for Australian retail businesses, 2019-20 to 2023-24



7 Conclusion

As the Inquiry moves into the next phase, Coles looks forward to continuing to work constructively with the ACCC and other stakeholders. Coles welcomes ongoing fact-based discussions about competition in grocery retailing and how competition and consumer outcomes can be enhanced in this sector that is so critical to the everyday lives of all Australians.

Appendix A – List of policy recommendations

(a) Customer experience

1. **Shrinkflation:** Coles is open to exploring measures to enhance customer transparency in relation to changes in weight or pack size as part of an industry wide solution, noting that any impacts to suppliers and Grocery Code compliance will need to be carefully considered.
2. **Clarity around promotional rules:** Coles submits that both competition and consumer outcomes in grocery could be enhanced by the ACCC publishing more detailed guidance on pricing and promotional claims. Compliance guardrails of this kind must strike the right balance between facilitating and restricting competitive pricing.
3. **Transparency of prices:** Coles considers that CHOICE's mystery grocery basket shop could play a more meaningful role in educating customers about price competition if the actual brands purchased as part of the mystery shop were disclosed to consumers.
4. **Unit pricing:** Coles is open to exploring options for improvements to unit pricing (noting the Federal Government's recent announcement of a review of the Code), such as requiring greater consistency with units of measurements and improving readability. Coles sees merit in the requirements being extended to other grocery retailers (potentially subject to a minimum size requirement) to further assist customers.
5. **Multi-buys:** Coles does not support policy measures which would in effect restrict price competition between retailers. Coles considers that multi-buys offer strong value to consumers, and they are one way Coles competes with bulk offers of grocery retailers like Costco and Bunnings. We would advise against restricting these, but agree that unit pricing should be clearly displayed.

(b) Suppliers

6. **Fresh produce volumes and pricing:** Coles supports the development of industry initiatives that would provide greater transparency of fresh produce market volumes and prices to growers, while avoiding potential competition law issues.
7. **Quality assurance:** Coles is aware that suppliers have raised concerns over the independence of our quality assessment processes. We have a responsibility to our customers to conduct rigorous quality assurance over fresh produce, and the quality team conducts these assessments independently. We would be open to recommendations by the ACCC that might enable suppliers to be assured of the independence of this process.
8. **Delisting decisions:** Coles notes Treasury's consideration of Grocery Code revisions following the Emerson Review. Coles believes that the current proposal to reverse the onus of proof such that normal commercial activities like making a decision to delist a product will be assumed to be an act of retribution against a supplier will have negative impacts on the efficiency of contracting, and make it more likely for retailers to seek supply from larger suppliers where displacing this assumption will be easier. Coles supports a well-defined Code that strikes the right balance between the fair treatment of suppliers and sustained best value for consumers.