Australian Competition and Consumer Commission

GROCERY PRICE INQUIRY HEARING

EXCERPTS FROM CONFIDENTIAL TRANSCRIPT OF WOOLWORTHS LIMITED

CONDUCTED AT: MELBOURNE CENTRAL TOWER, MELBOURNE

DATE: 10.00 AM, MONDAY, 19 MAY, 2008

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MR SAMUEL: Sorry, before you go off petrol vouchers. You've – and we've been through this in the context of the petrol inquiry, but I just wanted to look at some changes that you appear to have put into the system over more recent times, you are now moving towards a credit card type or electronic card concept?

MR LUSCOMBE: Yes, that's correct, yes.

MR SAMUEL: And that is ultimately intended to replace the paper coupons?

MR LUSCOMBE: Yes, it is, chairman.

MR SAMUEL: How long has that been around?

MR LUSCOMBE: We started after Christmas I think, no, no, before Christmas we did a trial for an extended period of time in an area around Orange in New South Wales to gauge how it would work, customer acceptance of it, whether they thought it was a good idea or not and it came back mostly positive, they actually don't like the dockets, they like the fact that they can get a card that they can link as many cards as they like. They can send a card to, you know, their cousin in Perth or, you know, their daughter at university somewhere and they can feed off rather than have to mail the dockets. That as well as that we obviously have given incentives for people to log on and sign up on line, rather than doing paper and we have, you know, I guess for want of a better word, a sweepstake, where we're offering, you know, free groceries on a regular basis, in stores, with a major prize in a state of $10,000 worth of groceries, etcetera.

So clearly what we've had is a loyalty program for many years, you know, the reward is the petrol voucher – petrol discount for their custom at our supermarkets and what we haven't been doing is collecting customer information to actually utilise it to help us market our business much better. I would have to say it's been amazingly popular, we already have nearly a million cards signed up on line and probably about one and a half million have been issued. There's no compulsion for anybody to obviously put their name and address down and they still get the ..... discount in the same way the voucher is, but the feedback we're getting is just beyond our expectations on the convenience of it. They just like having a card rather than having to deal with dockets that end up in the wash or get lost or blow out of the car window or whatever. They can always go on line and check their outstanding balance, etcetera.

MR SAMUEL: Now, in terms of the registration on line and you said that – I think you said that you've never collected data about your customer habits and the like - - -

MR LUSCOMBE: We have.

MR SAMUEL: I didn't want to sort of go into that so much as to the impact of the cards. If you register on line does that then enable you to record the purchases made by individual customers. In other words when they put their card through the sweep – whatever the system - - -

MR LUSCOMBE: Swipe.

MR SAMUEL: - - - they swipe it, that then indicates that you know Michael Luscombe's wife bought the following things on the following days and - - -

MR LUSCOMBE: Well, who had the card – we're presuming the card holder was the same person.

MR SAMUEL: Yes, yes, I understand that, yes.

MR LUSCOMBE: Yes, yes. Yes, that's right, yes, so that will help us understand in the way that fly-bys do for Coles-Myer and to be honest they're used by just about every other retailer round the world, we've just been late into it. We've always had a loyalty program in Tasmania.

MR SAMUEL: Right.

MR LUSCOMBE: Where most Tasmanians, even those that have left Tasmania are probably still members of our shopper club. We've also got one in New Zealand that's very successful as well. So we've been somewhat tardy in doing it in Woolies, but now we're moving into it.

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MR O'DONOVAN: You seem to suggest that it wasn't part of your business plan to improve pricing across the shop. Now, surely if there's a market opportunity to increase prices, then you, as a responsible CEO acting in the interests of your shareholders, will take that opportunity.

MR LUSCOMBE: Only if we're not achieving somewhere at least near our cost of doing business because in the end, what we want to do is to get a gross margin above our cost of doing business. So if, for any reason, we've got a product that's been, you know, the market has been down here and the market moves, then I won't anticipate they'd keep them, but I don't want them to go, you know, ... above because that's just not the way we want it to work. We're actually in the business of selling more and more because our big benefit is getting scale through our system. You know, it's actually how you manage the flow in our business that is the secret of success – the secret of Wal-Mart, the secret of Tesco, Parafrow, etcetera, has all been managing the flow of product and managing the amount of working capital in there at any one time. If you can do that well, then that gives you the ability to compete.

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MR O'DONOVAN: Sure, but if, for example, if you're a consumer who doesn't buy heavily promoted products like Coke, nappies, things like that, and just buys the general merchandise from Woolworths - - -

MR LUSCOMBE: Well, then they - - -

MR O'DONOVAN: - - - they're likely to be paying more - - -

MR LUSCOMBE: Well, no, no, no. Well, no - - -

MR O'DONOVAN: - - - and Woolworths is likely to be earning a better margin out of those consumers.

MR LUSCOMBE: Not necessarily. You know, we've taken the price of our bread down, our generic bread down, so they might – if they don't buy that, they might buy our private label. They may change to ..... so they're going to be much better off. They may have changed to rollback products.

MR O'DONOVAN: But generally speaking, it's true that if you're the kind of shopper who doesn't take advantage of those heavily promoted products, that Woolworths will be getting a better margin across the supermarket from those shoppers, or did. What this graph shows is that if there's a shopper who doesn't buy heavily promoted products, who has just been shopping at Woolworths across the board, Woolworths made a better margin out of them.

MR LUSCOMBE: That would be true of any retailer. Yeah, if someone bought only specials, they're not a great value customer.

MR O'DONOVAN: Sure.

MR LUSCOMBE: So you want a customer that actually buys a good mix of private label specials and standard prices. I can't think of too many studies that have shown any customers that don't buy any specials. I mean just, you know, with 4000 items on special, there's got to be a couple of products that you buy normally that's in your repertoire of products that are going to be, whether you like it or not it's going to be cheaper that week. You wouldn't say, "It's on special. I'm going to go buy the other product that's not on special". It doesn't happen.

MR O'DONOVAN: All right. Now, then moving on to generics. Now, it's fair to say that Woolworths consciously adopted a generic strategy.

MR LUSCOMBE: We've been into Home Brand since - - -

MR O'DONOVAN: Sorry, I should – private label strategy, I think. So I'm talking more broadly than just Home Brand.

MR LUSCOMBE: Okay, just to give you a bit of history, in general merchandise we've been in private label of one sort or another for many, many years. Woolworths actually had a private label, Woolworths brand and Safeway brand, back in the seventies and before then. They were discontinued when Home Brand came in as a generic in the early eighties, the first products. I, as leader of the supermarket team, our team made a proposal to the board or to the CEO at the time, a few years back that we should extend it away from a generic only private label offering to one that includes a two tier, so we have a premium and a generic. Coles would be a three tier where they've got a premium, a midstream and a generic, although they don't have too many of the premiums at this point of time.

We also moved that we moved into some functional specific type product, so we'll have Woolworths Organic, Woolworths Natura, Woolworths Freefrom, so free from sodium, free from gluten, etcetera. We also have got a number of private labels that we run in our general merchandise part of our supermarket business, home collection, etcetera, so they are not as well known, but we own the brands. In liquor we have a number of private label and control brands, so they are both brands that we own and have developed, but also we've got labels where we have exclusive rights to those brands within the country as if they were our own brands. In Fresh, we use just, you know, Woolworths Fresh as a marketing thing, generally speaking.

MR O'DONOVAN: All right, and it's true to say that this move into generics, I suppose, was initiated within the company, that there's a good business case for introducing it?

MR LUSCOMBE: Yes, that was the premise in which I represented on behalf of the team.

MR O'DONOVAN: Sure, and in terms of – it's clear what the benefits are to Woolworths in that it provides an opportunity for it to improve its margins within a category?

MR LUSCOMBE: Well, actually, one of the major premises that we put to the board and has been shown elsewhere, across the world, is that if you actually focus on the quality of the product, which has been our premise, so we haven't actually had any internal targets to say, we must have so many products or so much share of private label. Our focus has always been on delivering the best quality we can, we're visibly the market leader. What you actually build up is, it's another loyalty, because the only place you can actually buy those products are in Woolworths, so if I could just illustrate with one product group, it will give you a feeling for how, if you do it right, you can do it very successful, in nuts, [redacted] so one of our first products we put in was Select range of nuts, so we went – sent our buyers around the world to buy the best nuts we could in Vietnam and India, etcetera. We brought them back, we paid a company to grade them, to make sure we had the highest grade of, you know, intact and the right size and consistency in size. We engaged a company to actually cook the particular nuts, and also to develop seasonings that were unique to the marketplace, and then we developed a unique doily pack which is resealable, and we put the two together, and we put them on the shelf next to Nobby's, and within a short period of time, without any advertising, I think from memory they got to about 70 per cent market share of nuts within Woolworths.

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MR O'DONOVAN: Yes, all right. You generally won't choose to enter a category with a Select product unless its margin is an attractive margin, more attractive than you're earning on the branded products. That's right, isn't it?

MR LUSCOMBE: I can't think of anywhere where that's the – or that question has come into play, to be honest, not in my time, has it come in sense?

MR O'DONOVAN: The question of margin?

MR LUSCOMBE: No, no, no - - -

MR O'DONOVAN: You see, in the question of margin you can earn – surely that's always an issue, when you're choosing to enter into the Select market.

MR LUSCOMBE: No, not always. If I understand your question correctly, your question was, have you come across a situation where, if you put the Select in, you would earn a less margin than the market leader, and in that case, you wouldn't do it, is that how I understand it?

MR O'DONOVAN: I think you've got my question in reverse, but I suppose the simple – perhaps if I break it down this way. When you introduce the Select product, you consider what margin you can earn. That's a factor in deciding to introduce a Select product, gross margin?

MR LUSCOMBE: Eventually it is, the first thing we try and do is - - -

MR O'DONOVAN: No, no, let's not worry about eventually, but at some point in time, before it gets a tick to go ahead with introducing a Select product, you find out what margin you can earn on it?

MR LUSCOMBE: That would be right, yes.

MR O'DONOVAN: Yes, all right. It has to be a good margin for you to be interested in green lighting it, and by good I mean above [redacted] would you agree with that?

MR AYLEN: It needs – we desire to have a better margin than the market leader. We'd have a number of Select lines that do not make [redacted] per cent, in fact there's a couple that make a deal less than that, but that's reflective of the fact the market leaders in those categories make a whole lot less than that.

MR O'DONOVAN: Okay, so the goal in margin terms is to produce a better return in gross margin than the leader in that category?

MR LUSCOMBE: That would be one of the outcomes we want, yes.

MR O'DONOVAN: Okay, and in fact, that's – you won't proceed with introducing it unless it produces that result.

MR LUSCOMBE: I don't think we've come across that yet.

MR AYLEN: We haven't been faced with that question to say no, we won't proceed.

MR O'DONOVAN: Right, so by the time it gets to you guys, what's been worked up, fits the criteria that it actually – it earns a margin that's better than - - -

MR AYLEN: That's correct, Michael, our aim is to have Select at a higher margin than the brand of product, it's one of the criteria we look at.

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MR O'DONOVAN: Right. Well, I think we've come around to the point that the leading brand won't be able to deliver you a margin as good as Select, and Select would be able to be delivered to the customer at a lower price than the leading brand with a bigger margin.

MR LUSCOMBE: Correct. The customer wins and we win.

MR O'DONOVAN: Yes. All right, so from the point of view of the introduction to it, there's an obvious case for an improvement in returns for a shareholder, the Select case is one that can be justified just on shareholder grounds alone.

MR LUSCOMBE: That would be one reason, yes.

MR O'DONOVAN: Okay. But looking at it from a consumer's perspective, there are some disadvantages with this strategy in that it has led to the reduction in range and choice that's available at the Woolworths supermarket. Do you agree with that?

MR LUSCOMBE: On some categories.

MR AYLEN: I would argue it hasn't led to a reduction in choice, it has led to a different choice.

MR DONOVAN: Okay. So, consumers - but it's true to say that consumers who want to buy a preferred tea brand are now much more unlikely to find it in a category where there is a generic, select product, as a general rule, not in every case but that's true as a general proposition.

MR LUSCOMBE: We actually made a decision to go with the two tier and this was something that our previous CEO, Roger Corbett, was pretty strong on, and that it is that we actually believe one of the things that is important for us, is to actually have a range of choice, so our view of Tesco and others where they got very high private labels - and they got three and four tiered levels of private labels, is the shelves become pretty boring, because it's Tesco, Tesco, Tesco and you might only have one or two other brands. So we deliberately decided that we weren't going to play in the big field at the middle which is, you know, the You'll Love Coles field. We decided we were going to stick with 800 only home brands.

We'll do some niche things for products that don't actually exist, in most cases so Natura and Prefim, etcetera were because no one else was making them for us and we'll do the premium product of the level up the other end and we'll leave the middle ground for the brands including secondary and third brands. So we made a deliberate decision to do that. To say that Select can be in necessarily means that a brand disappears, isn't necessarily the case, it may mean that we, you know, we've got three Select products in a range. We might actually, you know, take the strawberry off one and the apricot off another brand and we'll make the room that way, or we may actually change the shelf configuration so we can actually fit more products on in that same space, subject to you know, the height, etcetera. If we've got some air gaps in our shelves, we might get an extra shelf in or we might change you know, the configuration of the equipment altogether. So it doesn't necessarily – but in some cases, it does.

MR O'DONOVAN: It's not necessarily so.

MR LUSCOMBE: In some cases it might, yes. Yes.

MR O'DONOVAN: And it's more than that, isn't it? That it's in many categories, there is now less choice for the consumer because Woolworths wants people to purchase the high margin - - -

MR LUSCOMBE: It's a different choice, so they've got – in most cases they've got a much better quality product at a lower price, so I think we've got – as James quite rightly put it, we've got a different choice, but I think it's a better choice because they've ended up with a much better product, quality-wise and we know that, and they're paying less for it, so we think it's actually a better choice for them.

MR O'DONOVAN: Sure.

MR LUSCOMBE: Now, they've got a much bigger choice and that is - if they can't find the product they want, they can go to the likes of an IGA that may actually stock that product and you know, many of our customers write to us and say, "look, you know" – well, not many but from time to time we get people saying, "Look, you've deleted someone's mandarin segments but I can get them at the local IGA which is around the corner" and you know, we have to then have to make a judgment, if enough customers write that in, we might put the mandarin's in if we - because if we don't, we run the risk that they'll take all their shopping round to IGA but we might say, "Well, this is a nice label for instance, and by the way we're selling one can per 20 stores per week anyway, so there are not too many people that really wanted this product anyway, so we'll just have to bear the consequences."

MR O'DONOVAN: All right, but in terms of what drives the decision to introduce Select – it's not demand from the consumers to have the Select product, it's a desire by Woolworths to earn a bigger margin in that particular category. Do you agree with that proposition?

MR LUSCOMBE: Well, I'll talk you through how it actually works. Basically what happens is that on a regular basis, the private labels then mix with James' team, so the business teams – so it might be that you know, the dairy team or it might be the pet food team or whatever, and they'll sit down and they'll say you know, what gaps have you got and what would you – you know, if you want a private label, what would you want? The business team will say, "Well, you know, there is no product that does x, y or z or one that delivers this, or one that has a can that opens this way or a packet that can be resealed," or whatever it may be. Then the private label team goes away and develops it or in some cases, they'll say, "Here are some concepts that we're thinking of, what do you think of these?" "That's good, we haven't got anything like that."

So they then come back with the finished products and by then, quite rightly we've worked out what the cost will be, we've worked out, you know, visibly the market leader, you know, we want to have a gap on it, what it sells at so that we've worked out what our margin will be. Typically, that's not going to be an issue and then we work with the business team to say, "Well, you know, we can have a range of 10 of these," and they might say, "Well, give us four to start with and over the next two years we'll rotate two flavours out, put two in, etcetera, etcetera. We'll need this much space and they'll say, "Okay, we can make that space, or we might need to make a deletion or we might need to cut – close back on the home brand a little bit," whatever it may be.

MR O'DONOVAN: Okay, but in terms of the offering that Woolworths wants to put in the category, or personally we do accept this – that the critical element and indeed one of the criteria that the business team has when they go away to work out the product, is that it will deliver the target margins that Woolworths has for its Select range. That's a fundamental criteria. It's not an accident that they come back with a product that happens to earn you an above average margin for the category.

MR LUSCOMBE: In terms of Select, what they've got to deliver first of all is the specifications and the product.

MR O'DONOVAN: Yes, and it's an essential element to a Select product, that it delivers a margin above the category average.

MR LUSCOMBE: Above the market leader.

MR O'DONOVAN: Yes.

MR LUSCOMBE: Market, not the category average, but the market leader.

MR O'DONOVAN: All right.

MR LUSCOMBE: Yeah.

MR O'DONOVAN: So that's part of the criteria when they go away?

MR LUSCOMBE: Correct.

MR O'DONOVAN: Okay, and then in terms of offering the – in terms of once you have identified that product, it's a decision then for Woolworths to move products out of the display shelves or whatever, and reduce the range of choices that the consumer has. You would agree that that's - - -

MR LUSCOMBE: Replace the change, replace the choice.

MR O'DONOVAN: Yes, so that's an essential component in the process of introducing the Select.

MR AYLEN: The challenge is on the word "reduce". If I have 40 items in a category and I replace a branded line with a Select line, I still have 40 items in the category. So I would not argue that I have reduced choice, I have maintained my choice, it is but a different choice and just one thing, making a great percentage is fantastic - - -

MR LUSCOMBE: You've got to sell it.

MR AYLEN: - - - but you've got to sell it and the only way you can bank dollars is if you can deliver the customer a product that their value equation on quality and price satisfies their desires to buy it and then you generate your GP, so it's great to have a great opening GP on Select but we have to produce a product that the customer needs to buy and wants to buy and does buy, to actually reap the reward of that actual program.

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MR LUSCOMBE: I would just say too, the introduction of Select in the end, for the business team is no different to the introduction of any new product, so on a regular basis, twice a year for most categories, we have a category review when we bring in new products anyway, so they will be the cause of deletions as well, and once again, they're just a different choice to what was there before. What we do do, in terms of changes of sizes of range is as we see categories becoming more important to customers or less important, we do globally bring back the number of products that we'll have and actually increase or decrease the space that we give a particular category. So you know, over time - if you think of Dairy Desserts in the dairy case, you know, there were virtually none and now there is swathes of them, obviously what we have a lot less of is space that we used to have for margarine, for you know, block cheese, etcetera. So over time, you know, categories actually expand and contract and there's deletions and new – commensurate new lines in other categories nearby that take up the slack. Is that B we're talking about? 10B?

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MR O'DONOVAN: Okay, then in terms of your relationship with Coles, is it true to say that it's not part of Woolworth' strategy to undercut Coles across the store? That it doesn't attempt to beat Coles pricing on the standard everyday items?

MR LUSCOMBE: We attempt to be – when we do our checks we actually get an overall report that talks about: on that basket of goods - you know, buy one of every one – are we cheaper or dearer? Our goal is to be in the negative and typically in most markets, most weeks, we are. If we are not, we identify the products that are causing this to be and we take them down. We don't typically take the other products up to balance the books. Then the other thing that we look at is: if we have checked 2000 prices, how many prices are the same or were the percentage of those prices the same - the percentage where they are dearer or we are dearer and we always want to get the balance of same and where cheaper, that percentage higher than the opposite. So we know that we won't be the same price on every product or cheaper than them on every product. It's just not possible but our aim is to be, on balance, slightly cheaper than they are. Typically on the reports that we get through from [redacted]

MR BATE: No, it's [redacted]

MR LUSCOMBE: [redacted] do it now. - I get each Monday afternoon to show that typically we are just slightly cheaper than Coles. We are substantially cheaper than the independent groups usually in the range of somewhere between two and five percent which is a substantial amount across a basket.

MR O'DONOVAN: Right.

MR LUSCOMBE: That's at standard shelf price too, by the way, it doesn't include specials.

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MR O'DONOVAN: Yes, so – and it will be fair to say that suggests that there is not fierce undercutting going on between you and Coles, is there?

MR LUSCOMBE: No, but once again you have got to take into account, you know, Coles came out and made a big virtue of the fact that they had two and a half thousand products on special each week. You might recall their campaign. Well, you know, at that same time, I think, our count was 4700. They had no products on rollback. This doesn't include rollback. This is just standard shelf price. So it's the whole basket that we are looking at including promotions, etcetera. So I wouldn't read from this that you can necessarily just say that the basket of goods is about the same because if everybody, you know, Coles and Woolworths, - you the equivalent customer buys the same number of products, on average we would have more products on promotion than they would. So the average basket should be cheaper.

MR O'DONOVAN: Sure.

MR AYLEN: Also, sorry, Mr O'Donovan. This is the relativity between Coles and our price. So if we drop prices and Coles react, the relativity would not change. It would show as a flat line. If they drop prices and we react, the relativity won't change. It would show as a flat line. So it doesn't truly reflect price movements, it purely reflects that we, basically, watch each other like hawks.

MR O'DONOVAN: So you think that there is - the absence of volatility is not suggestive that - - -

MR AYLEN: I don't believe the absence - - -

MR O'DONOVAN: Of weakness in competition.

MR AYLEN: I don't believe the absence of volatility necessarily reflects a weakness in competition. It could in fact reflect how competitive the two of us are against each others prices in the market place.

MR O'DONOVAN: Okay, so it's the standard argument that, "Our prices are the same because we are so competitive."

MR LUSCOMBE: I don't know if it is the actual answer.

MR SAMUEL: Yes, but if you take us back to our earlier discussion today, the other answer is that what you have is tacit co-ordination; that is, that you're watching each other like hawks and, you know, keeping your distance. And so what you're doing is, you're saying, "Well, we'll watch what Coles does and we'll match them." Coles is saying, "We'll watch what Woolies does and we'll match them," and guess what, you match each other without a great deal of pressure in terms of discounting. I think you did indicate that your store managers are not authorised to go below Coles across the broad baskets.

MR LUSCOMBE: That would be the case. Well, they are, because what we do, Chairman, is look at a whole host of competitors, not just Coles. In fact, if we do go below the Coles – they may actually come down to us, but if we pick up a price in Ritchies or in Franklins, etcetera, we – on an individual product – so if there's a cumulation on individual products we will go down.

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MR LUSCOMBE: [redacted] The whole premise of this is that we want to have a basket across the year – you know, we don't pretend we can physically be the cheapest on every product across the range; this is impossible. You know, not even Tesco would say that. Even on their website they list against the various competitors how many they're cheaper than and dearer than as well.

It's about delivering that whole basket, along with everything else that goes to why people choose to shop. You know, convenience, service, ambience, you know, cleanliness, etcetera, etcetera, etcetera; range, it might be private label that they like, or a particular retailer. Choice came to the same conclusion that our internal stuff said, and that is, price is important, but it's usually about number 4 or 5 in terms of the hierarchy of deciding where I'm going to shop.

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MR O'DONOVAN: [redacted] is telling us in fact is that there is quite soft competition between Woolworths and Coles, perhaps expressed in sales, perhaps the specials - there's intense competition to invest in particular special items – but across the store on all those – on the basic items that are not regularly put on special, competition is weak. Would you agree with that proposition?

MR LUSCOMBE: No, I wouldn't at all, no, not from where we sit. We actually see Coles as a very aggressive competitor.

MR O'DONOVAN: Right. And notwithstanding their aggression, you've been able to put up – improve your margin, which is partly being done by increasing your margin.

MR LUSCOMBE: Yes, by a number of means that we set out to do in '99/2000 through the investment that we did. We actually determined the cost improvements that we would make and we determined the margin improvements we would be able to make by re-engineering.

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Australian Competition and Consumer Commission

GROCERY PRICE INQUIRY HEARING

EXCERPTS FROM CONFIDENTIAL TRANSCRIPT OF COLES GROUP LIMITED

CONDUCTED AT: MELBOURNE CENTRAL TOWER, MELBOURNE
DATE: 10:06 AM, MONDAY, 26th MAY 2008

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THE CHAIRMAN: What would you say to a proposition that the rules haven't changed as far as the ACCC is concerned, the section 50 of the Trade Practices Act, but that the rules currently say if you acquire an asset that, and that includes a lease or a leasehold interest, if you acquire an asset and that has a likelihood of leading to a substantial lessoning of competition in a market, then the ACCC can prevent that asset being acquired. In other words, to put it in more commercial terms, that it's possible that the ACCC could turn around and say that the acquisition of that lease by Coles could be restrained on the basis that the combination of that with the restrictive covenant, breaches section 50 of the Trade Practices Act, or one or other of the sections, section 45 possibly as well.

MR McMAHON: If that was the case I would be very concerned, first of all, because we believe that what we do is obviously consistent with the law. We would take advice and we would respond on that basis.

MR PODDAR: Mr Chairman, may I interrupt on that point. I think it would be a very great question of whether that could possibly lessen competition substantially [redacted]

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MR O'DONOVAN: Okay. Would you agree with the assessment that it's – the Australian Grocery market is structurally attractive for a person buying into it?

MR McMAHON: [redacted] certainly we would see the Australian retail market as attractive. It's a stable economy. It's been growing for a long time. In comes Horizon. They're under pressure at the moment, obviously, but – and also that, you know, the food business is one that is resilient to downturns in the economy. So that would be our understanding of why this is an attractive market.

MR O'DONOVAN: [redacted]

MR McMAHON: [redacted]

MR O'DONOVAN: [redacted] I were to put that proposition to you that, because of those two factors, that it does have two major players, and that neither player has a history of unsustainable or excessive price discounting, makes it a relatively simple market to compete in?

MR McMAHON: It may be easier than some others for that reason, yes.

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MR O'DONOVAN: [redacted]

[redacted]

[redacted]

[redacted]

[redacted] in terms of your understanding, it is true to say, isn't it, that each of the major players and Coles and Woolworths have excellent information about each other's prices: that they both go out there and regularly, consistently obtain extensive information about each other's prices?

MR McMAHON: Yes.

MR O'DONOVAN: Okay. And as a consequence, whenever there is serious competitive conduct, it is promptly matched, or can be promptly matched, once it comes to the attention of the other player?

MR McMAHON: Yes.

MR O'DONOVAN: And as a consequence this effectively reduces the incentive for anyone to engage in this serious competitive behaviour, because it is immediately picked up, and the rewards for engaging in it are quickly lost, because the other player has such good information that they match it?

MR McMAHON: Well, I think if you take that to the nth degree, then there would be no promotions, there would be no price rewinds, there would be no House Brand, so I don't think that follows. I think there is a little bit of context that needs to be put on this, if I may?

MR O'DONOVAN: But just in relation to my question, you would agree that there is some disincentive, and indeed this is evidence of a disincentive for these really deep promotions?

MR McMAHON: No, I don't agree with that at all.

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MR O'DONOVAN: Okay. Now, the questions I have got relate to the pricing policy, and I suppose the detail of it. Now, as I understand it, there are, from your answers, that pricing is done at a national level, and I suppose at that first stage of the process the question is, what is the goal? Is there a goal to meet the competition at – in particular categories? Is it to undercut your competition in particular categories or across the board? Is it more explicit that, I guess, what we have been told here, which gives us a broad outline, but not a great deal of precision in terms of how that first cut is done.

MR McMAHON: Sure. Well, as we have said, we operate pricing at multiple levels, but at the first national level it comes more to what we are trying to do with the category, and whether the category is playing a role as a value driver, and whether the product within the category is seen as a value and traffic driver. Cameron, do you want to give a little bit of context, if you were placing a product at a price point within a category, what decisions the buyers might go through.

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MR O'DONOVAN: Right. Then moving down to the zone level, how many zones – how do you work out what a zone is? How do you describe a zone?

MR TRAINOR: Yes. A zone is a price structure that we assign stores into. It takes into effect the competitors that we compete with in those – in that immediate area and it's also used to help us in administration efficiency, because you could appreciate 27,000 products and the practical nature of our store managers doing that is just not on. So it's designed to help us from an efficiency perspective and also to ensure that we are competitive.

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MR O'DONOVAN: Okay. And then in terms of the, as I understand it, the store level, the stores have to specifically identify and have signed off who they are going to - - -

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MR TRAINOR: Nominate a competitor, yes.

MR O'DONOVAN: Nominate – yes, nominate a competitor.

MR TRAINOR: And I think we've provided you with all the stores nominated competitors around Australia.

MR O'DONOVAN: Right. Okay. And then in terms of – and once a store is a nominated competitor, then it is possible for the store manager then – is it only in respect of the key value items that they can shift to meet - - -

MR TRAINOR: Correct.

MR O'DONOVAN: All right. Now, in relation to the pricing of fresh food, does it operate in exactly the same way or does it operate differently?

MR STEVENS: The same principles, exactly the same principles.

MR O'DONOVAN: Right. So there's a price setting at a national level.

MR STEVENS: Yes.

MR O'DONOVAN: And then adjustment at a zone – state and zone level?

MR STEVENS: That's right.

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COMMISSIONER KING: All right. Well, seeing as we were just on fresh again, and I know we went through this earlier on but I just want to clarify for my own understanding and I think either of the two gentlemen who have experience with fresh can enlighten me. Can we go back to the story, I guess, if I can call it that – we've got two growers providing a product. On Wednesday the indicative prices go out, the product is delivered, it starts to come in. On Monday there is a view within Coles that there needs to be a reduction in price of that product to move more stock, for example. There might a view that, you know, currently Coles can't match the market based price point.

Of those two growers, you go back to them and say, "How about it? These are – we need to have a bit of a price reduction here". One grower says, "Fine. More than happy to do that", and the second grower says, "No, sorry, can't do". Then the next Wednesday, the tenders go out for that same product again for the next week. Now, as I understand your evidence, your evidence was that despite the fact that one of those growers had worked with Coles earlier in the week, and the other grower had not, the other grower had said, "Sorry, we are not helping you", there will be absolutely no difference in how Coles treats those growers on the Wednesday, after one of them has helped Coles and one of them has not. Is that what the evidence was that you gave earlier on?

MR STEVENS: Yes, it was.

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MR TRAINOR: What this would indicate to me, just quickly scanning it, is that the supplier of [redacted] – there is a couple of items being - in fact it looks like one item being deleted and there are two [redacted] products being added. And like any new line that we look to introduce we want to give it the best possible chance to succeed, because it is a costly exercise to add new lines as well as delete new lines, and we would have negotiated [redacted] a form of introductory deal that may have had – I haven't got the specific pricing behind it but it may have been reflected after the initial retail sell price had been established in terms of a special sell price or it may have been linked to some form of display [redacted] to support the new line [redacted] without, again, confirming the specific buyer, the understanding of that I imagine it would be around to help partially fund the clearance of some of the deletion items [redacted]

MR O'DONOVAN: [redacted]

MR TRAINOR: We ask the suppliers to support us with the, partially support us, [redacted] but we would ask the supplier in this case, because it is in the supplier's interests to get the new products to market as quickly as possible. We certainly wouldn't want to be taking a product out that's performing. It serves the suppliers no good. It is no good for us. It is certainly no good for our customers. So for this one we would be talking to [redacted] and we may run a good special on it to help move it through in terms of getting it out of the system, getting it out of the business as quick as we possibly can, to make way for the new products coming on the market.

MR O'DONOVAN: [redacted]

MR TRAINOR: [redacted]

MR O'DONOVAN: Right. And that's just – and that is, I suppose, negotiated as part of a continuing relationship?

MR TRAINOR: It is a commercial negotiation.

MR O'DONOVAN: Now, in terms of the terms that you are able to obtain from suppliers, this is more generally now, and that is in terms of things like the rebates that they offer or, I suppose, the percentage rebates that they offer for things like ullage and payment on – payment within a certain period and I think they have, sort of, direct to DC rebates and on fresh fruit and veg you also have percentage rebates which you ask for. Am I right in identifying all of those as possible - - -

MR McMAHON: We have a range of commercial arrangements with suppliers. We have set them out, both in answers to questions, and in fact in our supplementary submission we put in on Thursday or Friday. That's a huge topic. Is there one piece you would like to - - -

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Australian Competition and Consumer Commission

GROCERY PRICE INQUIRY HEARING

EXCERPTS FROM CONFIDENTIAL TRANSCRIPT OF WESTFIELD MANAGEMENT LIMITED

CONDUCTED AT: MELBOURNE CENTRAL TOWER, MELBOURNE

DATE: 10.09 AM, MONDAY, 12th MAY 2008

...SECTION OF TRANSCRIPT REMOVED DUE TO CONFIDENTIALITY ...

MR O'DONOVAN: All right. So if [redacted] came to you and said, look, we'd like to open a 3600 square metre large format supermarket, and you had a toss up between [redacted]

MR MILES: Yes.

MR O'DONOVAN: - - - is there any circumstances in which you would accept [redacted] as a tenant, if you genuinely had the choice, all other things being equal?

MR MILES: Well, all other things being equal, no, you probably wouldn't.

MR O'DONOVAN: Right, and what's the principal driver behind that?

MR MILES: Because they don't have a proven track record really in generating a strong enough level of sales out of that size box.

MR O'DONOVAN: And what would be the impact for Westfield in terms of all of its other tenants if it opted for an under-performing anchor tenant?

MR MILES: Well, you either wouldn't be able to lease the shops outside it to other fresh food retailers who we would normally put with the supermarket, or the mall that led to that supermarket would have less traffic because there would be less people going to that destination. And so either the ability to lease space in the first place would be much more difficult and/or you would lease at a lower rent which would mean you would question the overall viability of the scheme. [redacted]

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Australian Competition and Consumer Commission

GROCERY PRICE INQUIRY HEARING

EXCERPTS FROM CONFIDENTIAL TRANSCRIPT OF TEYS BROS (HOLDINGS) PTY LTD

CONDUCTED AT: MELBOURNE CENTRAL TOWER, MELBOURNE

DATE: 10.09 AM, MONDAY, 12th MAY 2008

MR SAMUEL: All right, we'll start. Thank you, everyone, for attending. My name is Graeme Samuel. I'm the Chairman of the Australian Competition Consumer Commission and the chair of this public inquiry into the competitiveness of retail prices for standard groceries. I welcome you all and declare the hearing open. I'm joined by Commissioner John Martin and Commissioner Stephen King who are the other two presiding members of the inquiry.

The inquiry has convened under part 7A of the Trade Practices Act. It's held pursuant to a request from the Assistant Treasurer and Minister for Competition Policy and Consumer Affairs, Minister Chris Bowen, which was received by the ACCC on 22 January 2008. Matters to be taken into consideration by the inquiry are set out on the website, which include the terms of reference that were provided to us by Minister Bowen.

I notice that the ACCC has so far received over 190 public submissions to the inquiry, as well as confidential submissions. We'll endeavour to take into account all of the information that has been provided and we do thank industry participants for the contributions that have been made. We understand that the competitiveness of retail grocery prices is of significant concern to all Australians. Now, the purpose of these hearings is to give the ACCC an opportunity to investigate in detail issues raised as part of the inquiry with industry participants. We've held hearings throughout Australia during April, with several hearings occurring in Melbourne throughout May and early in June.

I wish to emphasise that many witnesses at these hearings are not attending voluntarily and have been summonsed to appear under section 95S of the Trade Practices Act. In particular, I noted that in general the ACCC has summonsed all supplier companies. Therefore, no conclusions can be drawn regarding a company's willingness to participate in the inquiry from the fact that company is appearing at the hearings. Some of the material covered in hearing sessions will be confidential and commercially sensitive and, therefore, parts of the hearings will not be open to the public. Questioning will start in public but sessions will move into a confidential phase when the questioning moves onto confidential material relating to the witness.

The ACCC has to be able to investigate issues that are commercially sensitive to witnesses without damaging the witnesses' competitive position and commercial relationships. We'll be questioning organisations their commercial relationships and about confidential documents that the ACCC has obtained through using its information gathering powers. Now, clearly that cannot occur in public. In particular, where a witness has not made any submissions to the inquiry and has been summonsed by the ACCC to attend these hearings, we must be able to hear certain evidence in confidence. Transcript of the public parts of the hearings are placed on the ACCCs website. We may disclose some aspects of the confidential components of the transcript a while after the hearing if we consider that some of the material should be in the public domain, but we will consult with the relevant witness before doing this.

Where there are industry associations or representative organisations who are attending voluntarily, it is more likely that most of the hearing sessions will be in public. In terms of procedural issues all witnesses will have received a document that outlines how we intend to approach this hearing, so I won't go through those procedural points in detail. I just wish to emphasise that although we're not taking evidence under oath at this hearing it is a serious offence to give false or misleading evidence to the ACCC. A transcript of the proceedings, apart from any proceedings held in private and determined to be confidential by the ACCC and the witness involved at the inquiry, will be made available on our website.

Now, as I said before, we recognise that some witnesses will be asked to give evidence that if disclosed would damage their competitive position or which may for other reasons be confidential. If a witness believes that a particular person or a series – a particular question or a series of questions are likely to require him or her to disclose such confidential information, the witness should indicate an objection to answering the question on that basis. I will then consider whether the inquiry should take evidence in private from that witness. I note that although the ACCC is not utilising external counsel at this hearing, witnesses will be questioned by the ACCCs internal lawyers, Mr Damien O'Donovan, assisted by Ms Catherine Freeman.

That concludes my preliminary remarks. I thank all of the witnesses that are attending the hearings, particularly those that have been summonsed to attend. We realise that you are busy people and attending these hearings can be a significant imposition on you and your organisation.

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MR O'DONOVAN: Right. Okay. And, literally, when you're setting your price the question you're asking yourself is, what can we sell this overseas for, and will set your price based on that?

MR KIMPTON: Yes.

MR O'DONOVAN: Right. Okay. So it's truly an international commodity?

MR KIMPTON: Absolutely.

MR O'DONOVAN: Yes. Okay. And in terms of – and that's a completely distinct process from negotiating the grid with the pastoralists?

MR KIMPTON: That's separate. We don't – we don't have a philosophy of – but we work within the market on any given day. So buying the cattle, whatever the market dictates there, that's what we – that's where we have to go – go with if we want to buy the cattle. As far as selling the meat globally, then whatever the market dictates, well, then, obviously we're trying to get the best revenue we can on any given day, but we will go with the markets.

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MR O'DONOVAN: No. Okay. Now – all right. So, really, things like whether the labour market changes, or the price of fuel goes up, or the price of feed goes up, none of these things are directly relevant to how you set prices?

MR KIMPTON: They will all impact on our costs of production. So as the cost of production change, then we'll have to factor those into the business, but that will then determine the margins that we can achieve for the individual categories of cattle. And that will determine, depending on those margins, then that will determine what we buy, which way we go.

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MR O'DONOVAN: Right. Okay. And to what extent does the exchange rate influence where you want to sell?

MR KIMPTON: It's a major – well, it's a major influence and we – we're seeing it now, you know, where it is at the moment, up around 95 cents. That's having a major impact on the revenues we're able to get overseas for the product, therefore, that, then, flows back into the Australian market as well. That will – that determines what we'll sell back here as well.

MR O'DONOVAN: Okay. So has that put downward pressure on the domestic price of meat - - -

MR KIMPTON: Yes, yes.

MR O'DONOVAN: - - - at the wholesale level?

MR KIMPTON: It's kept prices down quite a bit.

MR O'DONOVAN: Right. Okay. So if the dollar was 50 cents, dropped to 50 cents US - - -

MR KIMPTON: Oh, prices would just double. They'd go right up, yeah.

MR O'DONOVAN: Okay. And is there any other factor that you can think of which dictates your price, or influences your price?

MR KIMPTON: No, because as far as the strategies are concerned we work with a spread in the – in the marketing system, a customer spread, and it – there's no, I'd say, probably no single customer has a major share of our business as far as sales are concerned.

MR O'DONOVAN: Okay. So the concentration at the retail level between – with Coles and Woollies having a very substantial share of the retail market, that doesn't translate into them having power over you in terms of the prices they can get?

MR KIMPTON: Not in any way at all.

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MR KIMPTON: We don't follow the retail prices. We do track the wholesale prices.

MR O'DONOVAN: Right. And what's the trend been in the wholesale prices?

MR KIMPTON: I'd say the wholesale prices now are cheaper than what I've seen for the last seven years.

MR O'DONOVAN: Right. And prior to – so has the trend been consistently down over the last seven years?

MR KIMPTON: No, it's just – it's basically gone – it's gone down over the last 12 months as the appreciating Australian dollar is driving it backwards.

MR O'DONOVAN: Right. Okay. And prior to that, was it trending upwards?

MR KIMPTON: Yes, yes. And we're able to maintain it at higher levels too throughout the year.

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