



Australian
Competition &
Consumer
Commission

Draft Notice

in respect of a notification lodged by

Nestlé Australia Ltd

Date: 3 April 2006

Notification no. N31488

Public Register no. C2005/1971

**Commissioners: Samuel
King
Martin
McNeill
Willett**

1. Introduction

- 1.1 The Australian Competition and Consumer Commission (the ACCC) is the independent Australian Government agency responsible for administering the *Trade Practices Act 1974* (the Act). A key objective of the Act is to prevent anti-competitive arrangements or conduct, thereby encouraging competition and efficiency in business, resulting in greater choice for consumers in price, quality and service.
- 1.2 Section 47 of the Act prohibits conduct known as exclusive dealing. Generally speaking, exclusive dealing involves one business which trades with another, imposing restrictions on the freedom of the second business to choose with whom, or in what, it deals.
- 1.3 Businesses may obtain immunity in relation to conduct that might be at risk of breaching the exclusive dealing provisions of the Act by lodging a 'notification' with the ACCC. Once lodged, immunity for the notified conduct commences automatically, except in the case of third line forcing conduct.
- 1.4 The ACCC may revoke a notification (other than in the case of third line forcing conduct) where it is satisfied that the conduct has the purpose, effect or likely effect of substantially lessening competition within the meaning of section 47 and it has not resulted or is not likely to result in a benefit to the public, or any benefit to the public that has resulted or is likely to result from the proposed conduct would not outweigh the detriment to the public constituted by any lessening of competition that has resulted from or likely to result from the conduct.
- 1.5 In effect, revoking a notification removes the immunity conferred by lodging the notification. The ACCC conducts a public consultation process before making a decision to revoke a notification.
- 1.6 The Act requires that, prior to issuing a notice revoking the immunity afforded under the notification process, the ACCC must first issue a draft notice setting out its reasons and providing an opportunity for interested parties to request a conference.
- 1.7 This document is a draft notice to revoke in relation to notification N31488 lodged by Nestlé Australia Ltd (Nestlé Australia) with the ACCC on 2 December 2005 in relation to conduct that may be in breach of section 47 of the Act.
- 1.8 Notification N31488 describes the conduct as:

Nestlé Australia proposes to enter into arrangements with ALDI whereby:

- *Nestlé Australia will supply NESCAFÉ BLEND 43 coffee and other Nestlé Australia products, as Nestlé Australia considers appropriate, to ALDI*
- *on the condition that;*

- *ALDI does not obtain from New Imports Pty Ltd or any other importer, distributor or wholesaler which competes with Nestlé Australia for the supply of soluble coffee products, “NESCAFÉ Classic Deluxe” or “NESCAFÉ Matinal” branded coffee, or similar types of coffee which Nestlé Australia considers to be of similar appearance and get-up as Nestlé Australia’s NESCAFÉ BLEND 43, without ALDI taking all reasonable steps to ensure that all promotions, advertising, marketing, point of sale, packaging or other such material in relation to those products expressly advises consumers that NESCAFÉ BLEND 43 is a unique coffee that is sourced, blended and roasted in a specific way to meet the sophisticated taste of the Australian market and is distinctly different from the “NESCAFÉ Classic Deluxe” and the “NESCAFÉ Matinal” branded coffee manufactured in Indonesia and Brazil respectively, such that Nestlé Australia customers are not under any misapprehension in relation to the product they are purchasing.*

2. Background

- 2.1 Nestlé Australia is an Australian registered subsidiary of the Swiss company, Nestlé SA. It is a manufacturer of food products, which it supplies to Australian retailers, and exports in conformity with Nestlé SA policies relating to sales into the territories of other Nestlé SA subsidiaries. According to AC Nielsen, in 2005 Nestlé Australia became the second largest grocery supplier in Australia, and the largest if suppliers of tobacco products are excluded.¹
- 2.2 ALDI Stores (ALDI) is a partnership, which has traded in Australia since January 2001. It operates in 12 other countries, and has a reputation as a “hard discounter” over a limited range of basic products. The range of goods and the service it provides is more limited than that provided by other grocery retailers. It currently operates 109 stores in New South Wales, Victoria, Queensland and the ACT; and it is still expanding its Australian operations.
- 2.3 For some time, ALDI has acquired products from Nestlé Australia including instant coffee (in particular Nescafé Blend 43), Milo and other branded products including Nestlé Killer Pythons and Nestlé Miniz. Nestlé Australia was also one of ALDI’s suppliers of non-branded products, including pizza, ice-cream and yoghurt.
- 2.4 In or around November 2005, ALDI commenced the retailing of Nestlé branded instant coffee products it had obtained from overseas suppliers. The products were branded Matinal and Classic Deluxe (the imported Nescafé instant coffee brands) and bore some similarities to the Blend 43 instant coffee product in respect of branding and the images used. In particular, Nescafé Classic Deluxe packaging bore some similarities with Nestlé Australia’s Blend 43 bearing a brown plastic cap and an image of a red mug on the label as does Blend 43.
- 2.5 In retailing the imported Nescafé instant coffee brands, ALDI highlighted the fact that the imported Nescafé instant coffee brands were imported and

¹ AC Nielsen Grocery Report 2005, p 10

different in comparison with the local Nescafé instant coffee brands in a number of ways:

- posters were placed above the displays of imported Nescafé instant coffee products, which said:

“everyday permanently low prices

\$4⁶⁹

CLASSIC TASTE INCREDIBLY LOW PRICE

To ensure consistent supply and a great price ALDI have sourced another superb Nescafé blend: Classic Deluxe 200g import. We believe it tastes just as good as Blend 43 at a more competitive price, offers satisfaction or your money back.”

- the same words apart from “everyday permanently low prices” appeared in ALDI’s catalogue.
- stickers, which were placed on the backs of the jars, saying

“INSTANT SOLUBLE COFFEE

Ingredients: Coffee Beans

Made in Brazil (in the case of jars of NESCAFÉ Matinal)

Imported by: New Imports Pty Ltd

151 – 163 Wyndham St, Alexandria NSW 2015

This is an Imported Product.

Composition and Taste of the coffee may differ to Local Product”

- shelf labels, which were of the same size as the price labels and placed next to the price labels, said

“Information

This Nescafe [Matinal/Classic] is sourced by ALDI from the International market, not from Nestle Australia. Whilst the blend is different to the locally sourced product we believe that the quality of the product is as good.”

This information was also displayed on larger labels placed above the shelves.

- Instructions were also provided to ALDI staff, so that they could explain the differences in the products to customers who enquired.

2.6 Becoming aware of ALDI's sale of imported NESCAFÉ instant coffee brands in November 2005, correspondence was exchanged between Nestlé Australia and ALDI in which Nestlé Australia required Aldi to:

- (a) *immediately withdraw the current unsatisfactory banner signage from its stores which are likely to mislead and deceive customers as to the origin and attributes of the Overseas Nescafé Brands;*
- (b) *affix and display very prominent stickers no less than 6cm by 6cm in size to be placed over the mugs on the front of the Overseas Nescafé Brands using the following words:*

This product is not supplied or endorsed by Nestlé Australia Ltd and has not been blended specifically for Australian tastes. This product is imported from overseas and has a different blend and taste to Nescafé Blend 43 coffee sold by Nestlé Australia Ltd in Australia.

The font size for the words "This product is not supplied or endorsed by Nestlé Australia Ltd and has not been blended specifically for Australian tastes" should be prominent, sans serif and not less than 5 mm in size.

- (c) *Replace the banner signage at point of sale in each Aldi store with banners of the same size containing the following words and no visual imagery:*

This product is not supplied or endorsed by Nestlé Australia Ltd and has not been blended specifically for Australian tastes. Nescafé Classic Deluxe / NESCAFÉ Matinal is imported from overseas and has a different blend and taste to Nescafé Blend 43 coffee sold by Nestlé Australia Ltd in Australia. Nescafé Blend 43 coffee is a unique coffee that is sourced, blended and roasted in a specific way to meet the sophisticated taste of the Australian market and is distinctly different from NESCAFÉ Classic Deluxe / NESCAFÉ Matinal* coffee.*

** Delete whichever product is not applicable in the relevant State in which the product is sold.*

The banner should be hung directly above any shippers or pallets containing Nescafé Classic Deluxe and Nescafé Matinal coffee in the same fashion as the current signage.

- (d) *Publish a full page front or back page corrective notice in the December 2005 edition of ALDI's store catalogue in New South Wales, Queensland and Victoria in the same terms as the corrective signage set out in (c) above, with the corrective notice also to appear on ALDI's website at www.aldi.com.*
- (e) *In addition, should Aldi wish to promote its Overseas Nescafé Brands in store or in its catalogue in the future, Nestlé requires that any marketing materials prepared for this purpose are submitted to Nestlé in advance for its review and written approval.*

- 2.7 Upon ALDI's failure to agree to the above requests, on 2 December 2005 Nestlé Australia lodged Notification 31488.
- 2.8 On 2 December 2005, Nestlé Australia wrote to ALDI informing ALDI that, as it had indicated it was not willing to take the steps requested by Nestlé Australia, Nestlé Australia would stop supply of all its products (including not only Nescafé Blend 43, but all other products including Nescafé Gold, Milo, a number of other Nestlé branded products and other unbranded products made for ALDI including dairy products and pizza) immediately, apart from any orders outstanding at that date and products which were supplied under contract. In the latter set of circumstances, Nestlé would give notice, pursuant to the terms of the contract, of its intention to cease supply at the earliest opportunity
- 2.9 On 2 December 2006 Nestlé Australia ceased supply to ALDI of Nescafé Blend 43, Nescafé Gold, and Milo, amongst other products.

3. Statutory provisions

- 3.1 Section 47 (1) of the Act provides that a corporation shall not engage in the practice of exclusive dealing. Section 47 then states that the practice of exclusive dealing includes the supply of goods or services on condition that the purchaser will not acquire, or will limit the acquisition of goods or services from a competitor of the supplier, where the condition has the purpose, effect or likely effect of substantially lessening competition.
- 3.2 Section 93 (1) of the Act provides that a corporation that engages or proposes to engage in conduct of a kind referred to in section 47 may give to the ACCC notice, as prescribed, setting out particulars of the conduct or proposed conduct. The effect of lodging such a notification is to afford protection to the corporation for engaging in the said conduct from legal proceedings under the Act.
- 3.3 Under section 93 (3) of the Act, if a corporation has notified the ACCC of conduct or proposed conduct of the type described in section 47 and the ACCC is satisfied that the conduct described in the notification has the purpose or has or is likely to have, the effect of substantially lessening competition within the meaning of section 47 and in all the circumstances:
- (a) the conduct has not resulted or is not likely to result in a benefit to the public; or
 - (b) any benefit to the public that has resulted or is likely to result from the conduct would not outweigh the detriment to the public constituted by any lessening of competition that has resulted or is likely to result from the conduct;

the ACCC may give a notice in writing stating that it is so satisfied and setting out its reasons in this respect. The effect of giving such a notice is to revoke the immunity afforded by lodging the notification.

- 3.4 Before revoking the immunity obtained by a notification, the ACCC must issue a draft notice of its intention (section 93A(1)) and give the applicant and interested parties the opportunity to respond and to call a conference (section 93A(2)) in relation to the draft notice.

4. Submissions received

Nestlé Australia's original submission

- 4.1 In lodging the notification, Nestlé Australia submitted that the imported Nescafé instant coffee products have similar labelling and overall get-up as Nescafé Blend 43, notwithstanding that these products are different from Nescafé Blend 43, including with respect to the source, blend and taste of the products.
- 4.2 It submitted that the notified conduct was not designed to stop the supply of imported Nescafé instant coffee products but rather to ensure that where they were supplied, that they were appropriately differentiated. It said that the differentiation it sought would benefit the public because it would alleviate any potential for consumers to be confused by the differences between Nescafé Blend 43 and the imported products.
- 4.3 Nestlé Australia further submitted that the conduct would not lessen competition in any relevant market because:
- the conduct was reasonable;
 - the conduct would not restrict or prevent the supply of overseas instant coffee products to ALDI or prevent the importation of such coffee products;
 - Nescafé Blend 43 is widely available in a large number of retail outlets which compete with ALDI, so the conduct would not have an adverse impact on the availability of those products, or on consumer choice; and
 - the conduct would promote consumer awareness, so that consumers were appraised of differences between the brands, particularly with regard to the source, blend and taste.
- 4.4 Nestlé Australia also submitted that the sales of products supplied by Nestlé Australia to ALDI were limited.

ALDI's submission

- 4.5 The ACCC received a submission from ALDI Stores on 12 January 2006.
- 4.6 ALDI submitted that it was important for retailers to stock Nescafé Blend 43 and Milo in order to compete effectively in the Australian retail grocery market. Nescafé Blend 43 and Milo, it said, were key products which a grocery retailer must stock. Without these two products ALDI would be limited in its ability to compete with the major grocery retailing chains. Not

only would it lose sales of those products, it would also risk losing sales of other unrelated products as consumers might be less inclined to shop at ALDI if key products were not available. ALDI also noted that the Nestlé Australia products accounted for the majority of ALDI's sales of instant coffee and nutritional milk modifiers (Milo).

- 4.7 ALDI submitted that it had experienced difficulty in its dealings with Nestlé Australia in respect of Nescafé Blend 43 coffee. It noted that in late 2004 and 2005, it became concerned that it was receiving stocks of these products on uncompetitive terms as to the price at which they were supplied, to the extent that ALDI was losing money on the sale of Nescafé brand coffee. ALDI also raised concerns over supply difficulties from time to time.
- 4.8 It advised that it had taken what it considered were adequate measures to differentiate the overseas Nescafé coffee brands from the Australian Nescafé coffee brands in order to ensure that customers were not confused as to the product they were buying. These measures are described in paragraph 2.5 above.
- 4.9 ALDI submitted that it believed that Nestlé had engaged in the conduct for an anti-competitive purpose, which was to discourage parallel imports of Nescafé branded products into Australia. The availability of these products would threaten Nestlé Australia's dominant position in the Australian instant coffee market.
- 4.10 It considered the notified conduct was punitive, in withdrawing supply of all Nestlé Australia branded and unbranded products, rather than just the one product which was allegedly the subject of potential customer confusion.
- 4.11 ALDI submitted that it considered the conduct would produce no public benefits, but rather would reduce consumer choice and diminish competition in the retail grocery market, both of which were detriments.

Nestlé Australia's response

- 4.12 Nestlé Australia lodged a submission on 9 March 2006 in response to ALDI's submission.
- 4.13 Nestlé Australia submitted that the conduct was neither punitive nor anti-competitive. Rather, the purpose of the conduct was to protect Nestlé Australia's brand and its product reputation, so that customers are fully appraised of the essential characteristics of the products they are buying. Its purpose, it stated, was not to limit parallel imports or to restrict ALDI's ability to compete in any relevant market.
- 4.14 They submitted that the conduct would have no adverse impact on consumers of soluble coffee. Nescafé Blend 43 was available in many other retail outlets, so consumers would not be denied the opportunity to purchase that brand of coffee. In addition, ALDI, by its own admission, had only a small share of the retail grocery market and was not price competitive against Coles and Woolworths in the supply of Nescafé Blend 43, so that even if no coffee was available in ALDI stores there would be no substantial

lessening of competition. Furthermore, if the overseas Nescafé coffee brands were effective substitutes for Nescafé Blend 43, their presence in the market ensured that the conduct did not substantially lessen competition. In any case, ALDI could source competing products from other Australian suppliers, from overseas suppliers, or manufacture its own house brand.

- 4.15 Nestlé Australia also submitted that the conduct would not lessen competition in the retail grocery market. It noted that ALDI has only 3.7% of the market for retail groceries in Australia, so that conduct affecting its capacity to compete would not substantially lessen competition in the retail grocery market. Nestlé reiterated the point that ALDI could source competing products from other Australian suppliers, from overseas suppliers, or manufacture its own house brand.
- 4.16 Nestlé Australia said that the conduct would produce public benefits in that it would alleviate confusion amongst consumers about the origins and taste of the overseas Nescafé coffee brands, which would avoid long term loss of value to the Nescafé brand and a loss of the trust that Australian consumers place in that brand. Nestlé Australia noted that the ACCC has previously accepted that the provision of better information to consumers and businesses is a public benefit, because it permits informed choices to be made.
- 4.17 Nestlé Australia submitted that a further public benefit would result from consumers being informed of the differences between brands.
- 4.18 Nestlé Australia said that there was no evidence of detriment arising as a consequence of the conduct, as there would be no lessening of competition. Nestlé Australia pointed out that the conduct made supply of Nescafé Blend 43 to ALDI conditional on ALDI taking certain steps with respect to its marketing of the overseas Nescafé coffee brands. Nestlé Australia reiterated that: there could be no substantial lessening of competition where ALDI was not prevented from sourcing coffee products from Australia or overseas, or from manufacturing a house brand; and there were a number of alternative sources of supply of Nescafé Blend 43 for consumers.
- 4.19 Nestlé Australia also sought to rebut ALDI's claims relating to wholesale pricing and continuity of supply of its products to ALDI stores.

5. ACCC Assessment

Market definition

- 5.1 To assist with necessary assessment of the purpose, effect or likely effect of proposed conduct on competition, it is helpful to identify the relevant markets affected. For the purposes of assessing this notification, the ACCC has considered the following markets:
- the market for the wholesale supply of instant coffee in Australia (the instant coffee market);
 - relevant retail grocery markets.
- 5.2 Having regard to the instant coffee market, the ACCC considered whether there existed a broader market for the wholesale supply of coffee products incorporating instant coffee, coffee beans and ground coffee products. Having regard to the price differential between the products and submissions from both ALDI and Nestlé Australia as to consumer preferences, the ACCC considers it is more likely that a narrower instant coffee market is appropriate. In any event, the ACCC does not consider its assessment would be overly affected by the wider definition.
- 5.3 On the other hand, the ACCC also considered whether there might exist a narrower market incorporating Nestle branded instant coffee. Again, both Aldi and Nestle submissions as to consumer preference support such consideration. Indeed, Nestlé Australia's ability to withhold supply of its product on condition that limitations are placed on supply of competing products suggests there may well be limited substitution for Nestlé branded products (such as Nescafé coffee and Milo). The ACCC does not have sufficient information available to determine whether a narrower market exists but notes that any such narrowing would be more likely to increase ACCC concerns as to anti-competitive detriment.
- 5.4 The instant coffee market appears to be national.
- 5.5 With respect to the retail grocery markets, the ACCC has had cause to consider similar market definitions previously. Market definition is purposive, meaning the market may be defined differently depending on the conduct being assessed. In some cases the ACCC has considered localised markets, in other cases it may be appropriate to consider a broader market.
- 5.6 Having regard to the retail markets identified, it is relevant to note that ALDI advises that it has a 3.7% share of the national packaged retail grocery market. It has obtained this market share in a little over 5 years, since it opened its first Australian store in January 2001.
- 5.7 With respect to the local geographic markets in the vicinity of each ALDI store, ALDI has approximately 109 stores in Queensland, New South Wales, Victoria and the ACT. It is not proposed to analyse the effect of each individual ALDI store on competition in its local geographic market, but some general conclusions can be drawn from the available evidence.

- 5.8 In general, the geographic catchment for each supermarket will vary, depending on the geographic and demographic characteristics of the area in which it is located. There may also be some overlap at the outer edges of each of these local geographic markets, so that strong competitive activity in one such market may also affect behaviour in neighbouring markets.
- 5.9 Given ALDI's current presence, and as it continues to expand its operations, regardless of the precise nature of market definition, it is clear that the relevant area of impact of the conduct in this case is much of eastern Australia.

Purpose of proposed conduct

- 5.10 Under section 93 of the Act, the ACCC may revoke a notification where the ACCC is satisfied that the conduct described in the notification has the **purpose** or has or is likely to have, the effect of substantially lessening competition within the meaning of section 47 of the Act and where it considers the conduct is otherwise not in the public interest. It is therefore relevant to consider Nestlé Australia's purpose with respect to the notified conduct.
- 5.11 A corporation will have the purpose of substantially lessening competition if that is its actual purpose for engaging in conduct.² This will be ascertained from direct and indirect evidence as to the actual intentions and purposes of the corporation.³ The Act provides that the relevant purpose must be a substantial purpose but not necessarily the sole purpose.⁴
- 5.12 Internal documents obtained from Nestlé Australia, but not otherwise placed on the public register, indicate that there were internal discussions involving relevant Nestlé Australia employees during November and early December 2005, in which those employees:
- raised concern over the impact ALDI's importation of Nescafé instant coffee brands would have on the brand value and profitability of Nestlé Australia and in particular its potential to encourage the competitive importation of instant coffee products;
 - indicated awareness of consideration by at least one larger Australian retailer to the possible importation of instant coffee products in order to compete with Aldi Stores;
 - sought advice as to the ability to limit ALDI Stores' importation of Nestlé branded instant coffee products, including efforts with Nestlé Singapore to locate the source of the imports; and
 - sought options available to cease the supply of Nestlé Australia products to Aldi Stores.

² *Universal Music Pty Ltd v Australian Competition & Consumer Commission* (2003) 201 ALR 636, at 693

³ *Ibid.*

⁴ *Section 4F of the Act*

- 5.13 The documents further demonstrate that, simultaneously, there were internal discussions involving relevant employees of Nestlé Australia that:
- identified consumer complaints concerning ALDI’s supply of Nestlé branded imported instant coffee products;
 - raised concern over the potential damage customer confusion may have for Nestlé Australia’s brand;
 - set out an aim, amongst others, to stop Australian consumers “trailing” the imported Nescafé instant coffee brands; and
 - resulted in the preparation of detailed plans to: differentiate Nestlé Australia instant coffee products from imported Nestlé branded instant coffee products; and to undertake necessary activities to avoid any consumer confusion or damage to the Nestlé Australia brand.
- 5.14 Nestlé Australia submits that the purpose of the notified conduct was to ensure that, where ALDI was to supply imported Nescafé instant coffee brands, such products were sufficiently differentiated from Nestlé Australia coffee products so as to avoid any consumer confusion or damage to the Nestlé Australia brand. In this regard, Nestlé Australia place some weight on the argument that it only required ALDI to cease supply of the imported Nescafé instant coffee brands where it would not agree to differentiate the products in the manner stipulated by Nestlé Australia.
- 5.15 The ACCC accepts that Nestlé Australia was concerned over the impact of ALDI’s supply of imported Nescafé instant coffee brands on the Nestlé Australia brand and possible customer confusion. This is demonstrated in the internal Nestlé Australia documents referred to above at paragraph 5.13.
- 5.16 The ACCC recognises that a manufacturer and distributor of goods has a legitimate interest in protecting the goodwill and trade reputation it has built over time in the markets in which it trades. The ACCC also considers that it is appropriate for manufacturers to seek to ensure that retailers do not engage in marketing practices that may mislead consumers in relation to the products supplied by those manufacturers. In some cases, where concerns over the manner in which the product is being marketed cannot be resolved, a supplier of goods may reasonably withdraw supply of its product from a retailer. In particular, it may be reasonable for a manufacturer to withdraw supply from a retailer which is unfairly comparing the supplier’s product with the product of the supplier’s competitors.
- 5.17 The ACCC does not, however, accept that Nestlé Australia provided ALDI with any real choice in relation to the continued supply of imported Nescafé instant coffee brands while still retaining supply of Nestlé Australia products.
- 5.18 The Nestlé Australia requirements set out at paragraph 2.6 above were made in an environment where ALDI had already – of its own accord – undertaken significant point of sale differentiation to identify the imported

nature of the products and the fact that they were not Nestlé Australia products (paragraphs 2.5 above refer).

- 5.19 Despite the lengths ALDI had gone to in order to differentiate the products, Nestlé Australia required further actions (paragraph 2.6 above refer) including corrective advertisements and point of sale representations which promoted Nestlé Australia instant coffee products at the expense of the imported Nescafé instant coffee brands and required Nestlé Australia approval for future advertising. The ACCC considers such requirements were not necessary or reasonable, and would not have been acceptable to any retailer.
- 5.20 More likely, having regard to the internal Nestlé Australia documents referred to at paragraph 5.12 above, the ACCC considers that a substantial purpose of the notified conduct was to deter ALDI from continuing to supply imported instant coffee products in Australia so as to:
- lessen the competition generated by ALDI's supply of products in competition with Nestlé Australia products; and
 - lessen the competition associated with the likelihood that other larger supermarkets would seek to supply imported instant coffee products (as Nestlé Australia believed such retailers were considering) in competition with ALDI.

Both of these would place downward pressure on the prices of Nestlé Australia instant coffee products.

- 5.21 As noted at paragraph 5.12 above, the ACCC considers internal Nestlé Australia documents identify a significant concern within Nestlé Australia over the potential for ALDI's importation of Nescafé instant coffee brands to lead to competitive responses from other larger retailers generating a significant competitive threat to Nestlé Australia instant coffee products. These documents further identify that Nestlé Australia sought options to limit ALDI's ability to import the said products or otherwise to cease Nestlé Australia's supply of products to ALDI.
- 5.22 The ACCC considers that the notified conduct was a mechanism by which Nestlé Australia believed it could discourage ALDI from supplying the imported Nescafé instant coffee brands either in the short or longer term. The ACCC considers that the notified conduct could also be intended to provide a signal to other retailers that might consider the importation of Nescafé instant coffee brands. In this respect, the refusal to supply Nestlé Australia's full range of products including flagship retail brands of Nescafé Blend 43 and Milo is likely to be seen by other retailers as strong discipline by Nestlé Australia.
- 5.23 The ACCC considers such purpose(s) to constitute a purpose of substantially lessening competition. In this respect, the ACCC is assisted by the Full Federal Court in Universal Music where they state:

“It is of particular significance that the appellants' conduct was a response to the first indication of parallel importation. This development opened the

possibility of intra-brand competition in price and quality and so on. The appellants' objective was to snuff out that competition before it gained a foothold. ... Nipping incipient small-scale competition in the bud was held to substantially lessen competition in *Rural Press* at [129] – [133]. This is applicable by analogy to the potential intra-brand competition here. Furthermore, as we have said, if the other major suppliers had independently taken the same position – a far from fanciful circumstance – success in whole or part was by no means out of the question. A new and disturbing element of competition was about to enter the market, of which there was no real experience. It would be expected that drastic defensive measures may be attempted by the incumbents, which may seem naïve in retrospect”.⁵

Effect or likely effect of proposed conduct

- 5.24 Under section 93 of the Act, the ACCC may revoke a notification where the ACCC is satisfied that the conduct described in the notification has the purpose **or has or is likely to have, the effect** of substantially lessening competition within the meaning of section 47 of the Act and where it considers the conduct is otherwise not in the public interest. It is therefore relevant to consider the effect or likely effect of the notified conduct.
- 5.25 To assess the effect or likely effect of conduct on a market, it is necessary to look at the relevant market, ask how and to what extent there would have been competition in the market but for the conduct, assess what is left and determine whether what has been lost in relation to what would have been if the conduct had not occurred, is a substantial lessening of competition.⁶
- 5.26 This requires the formulation of a counterfactual which can be compared with the state of competition in the market with the conduct. The ACCC believes that the appropriate counterfactual for the assessment of this conduct is a situation where ALDI was free to advertise and sell overseas Nescafé instant coffee brands while continuing to receive supply of the full range of Nestlé Australia products.
- 5.27 In submitting that the conduct would not lessen competition in any relevant market, Nestlé Australia argued, among other things, that the conduct did not prevent ALDI from continuing to import Nescafé instant coffee brands but rather that it only required ALDI to differentiate the products.
- 5.28 Assuming that this was the case, if ALDI had complied with the differentiation requirements set by Nestlé Australia the marketability of the parallel imports would have been significantly reduced. Consumers when presented with a choice of local and overseas products would be discouraged from exercising that choice in favour of the overseas Nescafé coffee brands. If successful, the measures would eliminate this source of competition before other retailers felt the need to respond to it by importing similar products. In consequence, Nestlé Australia's conduct in the instant coffee market would be less constrained than it would have been if the overseas Nescafé instant coffee brands were not required to be presented in a less attractive manner. The differentiation required by Nestlé Australia would to

⁵ Ibid

⁶ *Dandy Power Equipment Pty Ltd v Mercury Marine Pty Ltd* (1982) 64 FLR 238, at 259 - 260

a large extent neutralise the competitive advantage of the overseas Nescafé instant coffee products, so that customers would be less likely to purchase them despite the lower prices.

- 5.29 The conduct would increase ALDI's costs. Either it could import products and differentiate as instructed by Nestlé Australia, which would make the imported products less attractive to consumers, reducing sales and increasing the costs of importing and holding stocks of the imported products; or it could import and not differentiate, thereby losing supply of the Nestlé Australia products and the profit from sales of those products, especially Milo. This could also impact on the number of customers shopping at ALDI stores.
- 5.30 The ACCC considers that these outcomes would have the effect of substantially lessening competition in the instant coffee market.
- 5.31 In any event, as discussed at paragraph 5.19 above, the ACCC does not accept that ALDI was given any real choice in relation to continuing to supply imported Nescafé instant coffee brands while continuing to receive Nestlé Australia products. The differentiation actions required by Nestlé Australia, and the requirement that future advertising be approved by Nestlé Australia, would simply not have been acceptable to any retailer.
- 5.32 The attempts to impose onerous conditions on ALDI's presentation and advertising of the overseas Nescafé went beyond what was necessary to differentiate those products from the local Nescafé instant coffee products – particularly in the context of actions independently taken by ALDI to differentiate the products in question. The measures that Nestlé Australia sought to impose on ALDI were effectively advertisements for the local Nescafé instant coffee brands, especially Nescafé Blend 43.
- 5.33 On this basis, the ACCC considers that ALDI was faced with mutually exclusive decisions as to whether to continue to supply imported Nescafé instant coffee brands or to continue to receive the full range of Nestlé Australia products.
- 5.34 Nestlé Australia submit that in this regard ALDI comprises a small proportion of the relevant retail market and that consumers would continue to be able to acquire Nestlé Australia products from other retail outlets.
- 5.35 The ACCC accepts that ALDI's proportion of the relevant retail markets is a relevant consideration. It is an unusual case where it can be shown that competition in a generally competitive market has been or is likely to be substantially lessened by a refusal to supply one of a number of competitive retailers in the market with a product otherwise freely available and competitively marketed.⁷ The ACCC, however considers that the conduct otherwise has a substantial effect on competition in the instant coffee and retail markets having regard to the following matters.

⁷ *Outboard Marine Australia Pty Ltd v Hecar Investments No 6 Pty Ltd* (1982) 44 ALR 667, at 679 - 680

- 5.36 First, there is evidence to show that ALDI has a strong, positive effect on competition in retail grocery markets, which is disproportionately large for a participant with its market share. The presence of an ALDI store in a region creates significant price competition over a range of products.
- 5.37 AC Nielsen have recently reported that ALDI's growing market share has intensified price competition amongst supermarket chains.⁸ ALDI's presence has also fuelled the development of private label ranges by their competitors.⁹ These factors have put pressure on growth in the grocery sector, which requires a response from grocery suppliers.¹⁰ This has been particularly so in a market in which inflation in grocery prices has been low, and population increase has not been a strong source of growth in demand for groceries.¹¹
- 5.38 The ACCC concludes that each ALDI store is likely to have a significant effect on price competition in each of the local areas in which they operate. It follows that conduct which adversely affects ALDI's capacity to provide that price competition in each local geographic market will have an effect which is disproportionate to its market size.
- 5.39 Second, having regard to ALDI and Nestlé Australia, the ACCC considers that the importance of certain Nestlé Australia products to Australian retailers, particularly Nescafé Blend 43 and Milo, gives rise to greater competition concerns than might otherwise be the case.
- 5.40 ALDI's retailing strategy is built on stocking a narrow range of basic products which it sells at heavily discounted prices. Most of those products are ALDI house brands. ALDI representatives have stated their belief that, in order to compete in the Australian retail grocery market, there are a few brand name products which they are very important to stock. Two of those products are Nescafé Blend 43 and Milo. ALDI believes that if it cannot offer those products to its customers, some will abandon its stores in favour of competitors which consistently offer them. Given that some consumers are often "time poor", the absence of one key product from a preferred outlet, which necessitates a second trip to another store to acquire that product, is likely to cause consumers to shift their allegiance to the second outlet, even if it is more expensive.

⁸ "New product development and innovation now more critical than ever for consumer goods manufacturers", AC Nielsen, 12 January 2006, <http://au.acnielsen.com/news/20060112.shtml>

⁹ "High petrol prices start to bite into out-of-home dining budgets", AC Nielsen, 5 October 2005, <http://au.acnielsen.com/news/20051005.shtml>; "Food producers will rapidly slim down in 3 – 5 years KPMG predicts consolidation food fight", KPMG Australia, 29 November 2005, <http://www.kpmg.com.au/Default.aspx?TabID =214&KPMGArticleItemID=1632>

¹⁰ "New product development and innovation now more critical than ever for consumer goods manufacturers", AC Nielsen, 12 January 2006, <http://au.acnielsen.com/news/20060112.shtml>; *AC Nielsen Grocery Report 2005*, p 8; ; "Food producers will rapidly slim down in 3 – 5 years KPMG predicts consolidation food fight", KPMG Australia, 29 November 2005,

¹¹ "New product development and innovation now more critical than ever for consumer goods manufacturers", AC Nielsen, 12 January 2006, <http://au.acnielsen.com/news/20060112.shtml>

- 5.41 ALDI's belief that it is important to stock Nescafé brand coffee, and, preferably, the local Nescafé products, in the Australian retail grocery market, is demonstrated by its willingness to sell Nescafé Blend 43 at a loss over an extended period in order to make it available to ALDI's customers.
- 5.42 The fact that ALDI went to the effort described in the preceding paragraphs in order to obtain a product which it believed was a close substitute for the local NESCAFÉ products further allows the ACCC to draw an inference that supplies of these products or close substitutes were important to maintain ALDI's competitive status in the retail grocery market. Given the effect of ALDI's presence in the retail grocery market in the areas in which it operates stores, conduct which restricts its capacity to attract and retain customers has, or is likely to have, the effect of lessening competition in the retail grocery market.
- 5.43 Third, having examined the available evidence, including the submissions of ALDI and Nestlé Australia, and the internal Nestlé Australia documents, the ACCC concludes that the parallel imports of overseas Nescafé instant coffee brands were a source of substantial competitive tension in the instant coffee market. As revealed in internal documents, Nestlé Australia understood that ALDI's supply of these products had lead to advanced consideration by larger retailers to also import similar products. The ACCC considers that other retailer responses would also have been likely, such as further negotiations with Nestlé Australia with a view to lowering wholesale and consequently retail prices of Nestlé Australia instant coffee products.
- 5.44 As ALDI had only recently commenced the sale of these products when Nestlé Australia engaged in the conduct, sales of overseas Nescafé instant coffee brands were not a significant proportion of the instant coffee market. However, it is the degree to which competition has been lessened which is critical, not the proportion of that lessening to the whole of the competition which exists in the total market.¹² It follows that a lessening of competition in a significant section of the market, if it is a substantial lessening of active competition may be a substantial lessening of competition in a market.¹³ The level of interest with which other retailers responded to the arrival of a potential source of competitive advantage or threat indicates that the small market segment for overseas Nescafé instant coffee brands, which ALDI was creating, could have a substantial effect on competition in the wider instant coffee market.
- 5.45 The ACCC considers the notified conduct removed this competitive tension in the first instance by sending a clear message to retailers not to import Nescafé instant coffee brands for fear of losing the entire range of Nestlé Australia products.
- 5.46 While ALDI has to date chosen to continue to supply imported Nestlé instant coffee brands at the expense of receiving supply of the entire range of Australia Nestlé Australia products, this may not be possible in the longer term. Accordingly, while the conduct to date has not prevented ALDI from

¹² Ibid.

¹³ Ibid.

continuing to supply imported Nestlé instant coffee brands, the ACCC considers this position may not be viable in the longer term.

5.47 Having regard to each of the forgoing, the ACCC concludes that the notified conduct has or is likely to have the effect of substantially lessening competition in both the relevant instant coffee and retail grocery markets.

Public benefits

5.48 In the notification, Nestlé Australia submitted that the conduct would result in the following public benefits:

- it would alleviate any potential for consumers to be confused with respect to the source, blend and taste of NESCAFÉ BLEND 43 as compared to the overseas NESCAFÉ coffee brands;
- it would ensure that soluble coffee consumers were adequately informed about their products at the point of purchase, and, in particular, that consumers of soluble coffee were aware that the overseas NESCAFÉ coffee brands were not supplied or endorsed by Nestlé Australia.

5.49 The ACCC recognises that public benefits can arise from the provision of more information to consumers in a clear and explicit manner at the point where they make decisions to purchase goods. As discussed at paragraph 5.16, the ACCC considers that it may be appropriate to require product differentiation in some cases.

5.50 Having regard, however, to the extent to which ALDI had independently taken steps to differentiate the imported Nescafé instant coffee products from Nestlé Australia products, the ACCC is of the view that the Nestlé Australia requirements for further differentiation exceeded what was needed to provide consumers with adequate information on which to base their decision making at the point of purchase. Little, if any, additional benefit for consumers flowed from the material that Nestlé Australia sought to impose on ALDI as an appropriate level of disclosure.

5.51 The public benefits of the conduct must also be balanced against the removal of a range of choices for consumers in either the short or the longer term. New products were being made available for consumers to sample. These products may have met with a favourable response, or consumers may have rejected them. The conduct of Nestlé Australia will remove that choice. Indeed, internal Nestlé Australia documents also revealed that one of the aims of Nestlé Australia's plan to protect its brand was to prevent consumers from 'trailing' the imported Nescafé instant coffee products.

5.52 The ACCC concludes that the notified conduct generates little if any public benefits.

6 Draft Notice

6.1 For the reasons identified above, the ACCC considers that the conduct has the purpose, effect or likely effect of substantially lessening competition and the benefits do not outweigh the detriments. As a result, the notification lodged by Nestlé Australia on 2 December 2005 should be revoked.

6.2 The ACCC holds the view that Nestlé Australia engaged in the notified conduct for purposes including the purpose of substantially lessening competition in the instant coffee market because:

- it would diminish ALDI's sales of the imported Nescafé coffee brands, thereby eliminating a new source of competition for the Australian Nescafé instant coffee brands;
- it would remove the stimulus to other Australian retailers who might respond to ALDI's sale of the imported Nescafé coffee brands by importing the same or similar products;
- the conduct would send a signal to other retailers not to sell the imported Nescafé coffee brands.

6.3 The ACCC also holds the view that the conduct has the effect or likely effect of substantially lessening competition in relevant retail grocery markets and the instant coffee market because:

- ALDI has a strong positive effect on price competition, which would be reduced if ALDI could not stock certain key products manufactured by Nestlé Australia;
- it added to ALDI's costs of offering the imported Nescafé instant coffee brands for sale in Australia;
- it will remove a source of considerable competitive tension from the instant coffee market, which had quickly elicited a vigorous response from other, major, grocery retailers.

6.4 The ACCC believes that the notified conduct is disproportionate to what was needed to avoid consumer confusion, and that ALDI's actions to differentiate the products were adequate. Therefore, the avoidance of customer confusion cannot, in the ACCC's view, be claimed as a benefit of the conduct. The ACCC believes that there are no other public benefits resulting from the conduct.

6.5 As a result, the ACCC is satisfied that the conduct described in the notification has the purpose or effect, or is likely to have the effect, of substantially lessening competition and that the benefits do not outweigh the detriments.

6.6 Accordingly, the ACCC proposes to issue a notice to revoke the notification lodged by Nestlé Australia on 2 December 2005.