



Australian
Competition &
Consumer
Commission

Notice

in respect of a notification lodged by

Nestlé Australia Ltd

N31488

Date: 3 August 2006

Notification no. N31488

Public Register no. C2005/1971

**Commissioners: Samuel
King
McNeill
Smith
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 for conduct that might breach the exclusive dealing provisions of the Act, by lodging a ‘notification’ with the ACCC. Once lodged, immunity for the notified conduct commences automatically and immediately, 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 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.
- 1.5 Revoking a notification removes the immunity conferred by 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 then provide an opportunity for interested parties to request a conference.
- 1.7 On 2 December 2005, Nestlé Australia lodged notification N31488 describing 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.*

- 1.8 The ACCC issued a draft notice on 3 April 2006 proposing to revoke notification N31488 lodged by Nestlé Australia Ltd on 2 December 2005 in relation to conduct that may be conduct of a kind referred to in section 47 of the Act. A pre-decision conference was conducted on 11 May 2006, and interested parties have lodged further submissions.
- 1.9 This document is the notice, issued under section 93 (3) of the Act, revoking notification N31488.

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 grocery 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 approximately 120 stores in New South Wales, Victoria, Queensland and the ACT; and it is still expanding its Australian operations.
- 2.3 Prior to December 2005, ALDI acquired products from Nestlé Australia including instant coffee (including Nescafé Blend 43), Milo and other branded products such as 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 began to retail Nestlé branded instant coffee products it had obtained from overseas suppliers. The products were

¹ AC Nielsen Grocery Report 2005, p 10

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 to Nestlé Australia's Nescafé Blend 43, with a brown plastic cap and an image of a red mug on the label.

2.5 In retailing the imported Nescafé instant coffee brands, ALDI advertised the fact that the imported Nescafé instant coffee brands were imported, and differed in comparison with the local Nescafé instant coffee brands in a number of ways. ALDI had taken a number of measures to differentiate the imported Nescafé instant coffee products from the products of Nestlé Australia:

- 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 When ALDI did not comply with the above requests, Nestlé Australia lodged Notification N31488 on 2 December 2005.
- 2.8 On 2 December 2005, Nestlé Australia wrote to ALDI informing it that, as ALDI had indicated it was not willing to take the steps requested by Nestlé Australia (referred to at paragraph 2.6 above), Nestlé Australia would stop supply of all its products (including Nescafé Blend 43, 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 relation to the products supplied under contract, Nestlé Australia gave notice, pursuant to the terms of the contract, of its intention to cease supply at the earliest opportunity.
- 2.9 On 2 December 2005 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 provides 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. Such exclusive dealing conduct will only breach section 47 of the Act where it 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 from legal proceedings under the Act for engaging in the conduct.
- 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 remove the immunity afforded by lodging the notification.

- 3.4 Before issuing a notice 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 call a conference (section 93A(2)) in relation to the draft notice.

4. Submissions received

Submissions prior to the draft notice

Nestlé Australia's original submission

- 4.1 In lodging the notification, Nestlé Australia submitted that the imported Nescafé instant coffee brands have similar labelling and overall get-up as Nescafé Blend 43, notwithstanding that these products differ from Nescafé Blend 43, including with respect to their source, blend and taste.
- 4.2 It submitted that the notified conduct was not designed to stop the supply of imported Nescafé instant coffee brands but rather to ensure that, where they were supplied, 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 imported instant coffee brands 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 apprised 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 grocery 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 Australia 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 8 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 informed of the essential characteristics of the products they bought. Its purpose, it stated, was not to limit parallel imports or to restrict ALDI's ability to compete in any relevant market.
- 4.14 Nestlé Australia 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, it submitted that, 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

imported Nescafé instant 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 Australia 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 imported Nescafé instant 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 It 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 imported Nescafé instant coffee brands. Nestlé Australia reiterated that: there could be no substantial lessening of competition if 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.

Submissions following the draft notice

- 4.20 The ACCC issued a draft notice on 3 April 2006, proposing to revoke the notification. ALDI lodged additional submissions after the draft notice was issued. A pre-decision conference was called, and both Nestlé Australia and ALDI made further submissions after the conference. These submissions are summarised below. Substantive matters raised in those submissions and at the conference will be discussed issue by issue at relevant points in the section on the ACCC's assessment of the conduct.

ALDI's submission

- 4.21 ALDI lodged two submissions on 18 April 2006. One of these submissions has been excluded from the public register, having regard to the commercially sensitive nature of the material it contains.
- 4.22 ALDI informed the ACCC that evidence of promotional activity conducted by Nestlé Australia after ALDI began to sell the imported Nescafé instant coffee brands supported the conclusion (stated by the ACCC in the draft notice issued on 3 April 2006) that the imported Nescafé brands were a source of substantial competitive tension in the instant coffee market. ALDI particularly noted a \$3 cash back offer made by Nestlé Australia in February 2006, and the use of promotional material which asserted that Nescafé Blend 43 was sourced and blended specifically for Australian tastes.
- 4.23 In response to a submission from Nestlé Australia which described a number of customer complaints it had received about the imported Nescafé instant coffee brands, ALDI noted that, since it began to sell these products, there had been no reported instances of customer complaints to ALDI about the imported Nescafé products. Neither had ALDI received any written complaints about these products.

Pre-decision conference

- 4.24 Nestlé Australia requested a pre-decision conference, which was conducted on 11 May, 2006.
- 4.25 In its submissions at the conference, Nestlé Australia emphasised its concerns about product differentiation, the need to protect its goodwill and brands, and the avoidance of customer confusion as the motivations for lodging the notification. It also emphasised that the language used in the notification was not designed to, and did not in effect, stop ALDI from importing other Nescafé instant coffee products from overseas or from purchasing Nescafé Blend 43 from Nestlé Australia. The description of the conduct given in paragraph 5.14 of the ACCC draft notice was particularly criticised. On these bases, Nestlé Australia also questioned the ACCC's conclusions regarding the purpose of the conduct.
- 4.26 Nestlé Australia thought the differentiation requirements were not onerous, contrary to the description used in the ACCC draft notice. The complaints received by Nestlé Australia were referred to as evidence of actual customer confusion and potential damage to the goodwill of Nescafé Blend 43. It noted that ALDI had threatened in July 2005 not to stock Nescafé Blend 43, and argued that this undercut ALDI's arguments.
- 4.27 ALDI's submissions at the conference recognised the quality of the products supplied by Nestlé Australia. Nescafé Blend 43 was an icon and ALDI's best selling coffee for that reason. ALDI wanted to stock this product. It had only obtained imports after it encountered difficulty in obtaining continuous supplies of Nescafé Blend 43 on terms it considered appropriate. ALDI based the decision to stock Nescafé Blend 43 on the expertise of employees who had worked in Australian grocery retailing. These employees concluded that it was a "must have" item that ALDI must sell.

ALDI believed that it had gone to extraordinary lengths to differentiate the imported Nescafé instant coffee products from the local ones, and that there was no confusion about the products. ALDI was confident that the differentiation strategies were being complied with by individual stores, but 100% compliance by individual stores is not easily guaranteed.

- 4.28 The loss of supply of Nestlé products was damaging to ALDI. Finding replacements had been time-consuming, irrespective of ALDI's resources. ALDI supported the ACCC's description of the conduct in paragraph 5.14 of the draft notice. ALDI also noted that all Nestlé products had been withdrawn in a dispute that concerned only one product.

Nestlé Australia's submission following the conference

- 4.29 Nestlé provided a submission in response to the Draft Notice on 2 June 2006, raising the following matters²:

- Nestlé Australia's purpose was to differentiate its own products from the imported products in order to avoid customer confusion.
- The notified conduct does not have the effect or likely effect of substantially lessening competition.
- It questioned the ACCC's market definitions and the counterfactual.
- Actual consumer confusion provided evidence that ALDI's measures were inadequate.
- The ACCC provided no evidence of any public detriment. The public benefits outweigh the public detriments.

ALDI's submission following the conference

- 4.30 ALDI responded to Nestlé Australia's submission on 16 June 2006, addressing the following issues:

- The status of Nescafé Blend 43 in the retail grocery market
- The reason for obtaining imports, and customer response to them
- The get-up and differentiation of the products
- Customer complaints about the imported Nescafé coffee
- Purpose, effect and likely effect of the notified conduct
- Nestlé Australia's power in the relevant markets
- ALDI's role in the Australian retail grocery market and the effect of the notified conduct.

Nestlé Australia reply to ALDI's submission

- 4.31 Nestlé Australia responded to ALDI's submission on 30 June 2006. It made the following points:

- ALDI had not provided evidence to substantiate its claims.

² 2 June submission, pp 1 - 2

- The purpose of the notification was to ensure that there was adequate differentiation. It was not to stop imports. It also had no anti-competitive effects. Nescafé Blend 43 and Milo are widely available. They can be obtained by ALDI from third party distributors, and by customers at other grocery retailers.
- The notified conduct produces public benefits which can be substantiated with evidence of actual customer confusion.
- The differentiation required by Nestlé Australia is reasonable and the ACCC has not placed sufficient weight on actual evidence of consumer confusion.
- ALDI's differentiation measures were not being fully complied with in some of its stores.

4.32 Nestlé Australia provided a further letter making submissions on 31 July 2006.

5 ACCC Assessment

5.1 The ACCC must assess the notification by applying the test provided for in section 93 (3) of the *Trade Practices Act* (set out in 3.3 above).

Market definition

5.2 To assist with the assessment of the purpose, effect or likely effect of proposed conduct on competition, it is helpful to identify the relevant markets that may be 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);
- localised grocery retail markets across much of eastern Australia.

5.3 Having regard to the instant coffee market, the ACCC considered whether there is 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 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.

5.4 The instant coffee market appears to be national.

5.5 In its draft notice, the ACCC considered whether there might exist a narrower market incorporating Nestlé branded instant coffee. The ACCC noted submissions as to consumer preference and the actions of parties in the market. Ultimately, the ACCC did not conclude that such a narrower market exists.

5.6 Nestlé Australia has submitted that the ACCC was mistaken in discussing the possibility of a narrow market for Nestlé branded instant coffee in its

Draft Notice.³ To be clear, the ACCC does not claim that there is a narrow market for the supply of brand specific instant coffee.

- 5.7 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.
- 5.8 In this instance, noting that the conduct is directed towards Aldi stores, the ACCC has considered the notified conduct having regard to its effect on the localised grocery retail markets in which each Aldi store competes.
- 5.9 It is relevant to note that ALDI advised that it has a 3.7% share of national packaged retail grocery sales. It had obtained this share in a little over 5 years, since it opened its first Australian store in January 2001. ALDI has approximately 120 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.
- 5.10 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.
- 5.11 Given ALDI's current presence, and as it continues to expand its operations, regardless of the precise nature of the market definition, it is clear that the relevant area of impact of the conduct in this case is much of eastern Australia.
- 5.12 Nestlé Australia submits that the ACCC has ignored market definitions used in other recent matters relating to the Australian retail grocery market. It particularly notes the ACCC's published views in the Coles shopper docket and the Woolworths/Action acquisition matters. It emphasises that the ACCC adopted the position in these matters that Coles and Woolworths are the dominant participants in the Australian retail grocery market. Nestlé Australia also challenges the emphasis placed on ALDI in the Draft Notice.
- 5.13 The ACCC considers that the market definitions applied in this matter are not inconsistent with market definitions used in other assessments relating to the retail grocery markets.
- 5.14 The ACCC notes that the market definition it has adopted for retail groceries is similar to the recent decision of the Federal Court in *ACCC v Liquorland (Australia) Pty Ltd*⁴ where the Court found that the relevant markets were a number of separate and geographically limited retail markets.⁵

³ 2 June submission, p 5

⁴ [2006] FCA 826

⁵ Ibid, at para 423

5.15 It is also relevant to note internal Nestlé Australia documents support the view that competitive restraints in the relevant grocery retail markets are somewhat localised. In a power point presentation dated 11 November 2005, it was considering competitive responses "... only in stores within Aldi catchment areas to compete with import."

The notified conduct

5.16 There has been some debate as to the nature of the notified conduct.

5.17 At paragraph 5.14 of its draft notice, the ACCC referred to the notification as requiring that, where ALDI wanted to supply imported Nescafé instant coffee brands, it must differentiate the products from Nestlé Australia coffee products as required by Nestlé Australia. The ACCC stated that Nestlé Australia had placed some weight on the argument that it only required ALDI to cease supply of the imported Nescafé instant coffee brands if ALDI would not agree to differentiate the products in the manner stipulated by Nestlé Australia.

5.18 Nestlé Australia has contested this description of the notified conduct. It notes the differences between this summary and the language of the notification, which is reproduced in Section 1.

5.19 Nestlé Australia submits that the notification never required ALDI to cease the sale of the imported Nescafé coffee.

5.20 Nestlé Australia submits that the language used in the notification does not require ALDI to stop the supply of imported Nescafé instant coffee brands. Nestlé Australia considers that the notification left ALDI with choices and decisions.⁶

5.21 The ACCC agrees that the notification left ALDI with choices and decisions. These were as follows:

- ALDI could continue to source imported Nescafé instant coffee brands, but to alter the packaging and marketing of those products in the manner prescribed by Nestlé Australia, in order to obtain supply of Nescafé Blend 43 and other products from Nestlé Australia (the first option).
- It could continue to import Nescafé instant coffee brands, without altering the packaging and marketing in the manner prescribed by Nestlé Australia and accordingly lose supply of Nescafé Blend 43 and other products from Nestlé Australia (the second option).
- It could stop importing Nescafé instant coffee from overseas and continue to obtain local products from Nestlé Australia (the third option).

5.22 Ultimately Aldi took the second option.

⁶ 2 June 2006 submission, p 1

5.23 Section 93 of the Act requires that conduct the subject of a notification must be of a kind described in section 47 of the Act. Any suggestion from Nestlé Australia that the notified conduct did not involve a condition restricting (even to a limited extent) ALDI's acquisition of product from another person would place at risk the validity of the notification.

Purpose of notified 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 Nestlé Australia's purpose for engaging in the notified conduct.

5.25 A corporation will have the purpose of substantially lessening competition if that is its actual purpose for engaging in conduct.⁷ This will be ascertained from direct and indirect evidence as to the actual intentions and purposes of the corporation.⁸ The Act provides that the relevant purpose must be a substantial purpose but not necessarily the sole purpose.⁹

5.26 Having regard to internal Nestlé Australia documents, for the reasons discussed below, the ACCC considers that a substantial purpose of the notified conduct was to deter ALDI from continuing to supply imported Nescafé 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 grocery retailers would seek to supply imported instant coffee products (as Nestlé Australia believed such grocery retailers were considering) in competition with ALDI.

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

5.27 In its draft notice, the ACCC expressed the view that internal documents obtained from Nestlé Australia 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;

⁷ *Universal Music Pty Ltd v Australian Competition & Consumer Commission* (2003) 201 ALR 636, at 693

⁸ *Ibid.*

⁹ Section 4F of the Act

- indicated awareness of consideration by at least one larger Australian grocery 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.

5.28 The ACCC also noted that the documents demonstrated 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.

5.29 Nestlé Australia submits that the ACCC has erred in its assessment. It argues that the differentiation undertaken by ALDI was insufficient, that consumers were being misled, that its differentiation requirements were reasonable and that its purpose was not an anti-competitive one but to avoid customer confusion. Nestlé Australia challenges the ACCC's interpretation of its documents, claiming the ACCC had no basis for its conclusions.

5.30 The ACCC maintains its interpretation of the internal documents. Where relevant throughout this assessment, the ACCC has now included references to the documents to support its conclusions.

Customer Confusion and protection of brand reputation

- 5.31 Nestlé Australia submits that the purpose of the notified conduct was to ensure that, where ALDI was to supply imported Nescafé instant coffee products, such products were sufficiently differentiated from Nestlé Australia coffee products so as to avoid any consumer confusion or damage to the Nestlé Australia brand.
- 5.32 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 to some extent in the internal Nestlé Australia documents referred to above at paragraph 5.28.
- 5.33 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.
- 5.34 A supplier of goods may, in some circumstances, reasonably withdraw supply (at least from a competition law perspective) of its product from a retailer where the manufacturer's concerns over the manner in which the product is being marketed cannot be resolved. In particular, in some circumstances, it may be reasonable for a manufacturer to withdraw supply of a product from a retailer which is unfairly comparing the supplier's product with a product of the supplier's competitors.
- 5.35 The ACCC does not, however, consider Nestlé Australia's documents or actions support the view that concern over consumer confusion was the driving force or only purpose behind Nestlé Australia's conduct.
- 5.36 The ACCC considers that the differentiation requirements were so onerous that Nestlé Australia provided ALDI with no real choice in relation to the continued supply of imported Nescafé instant coffee brands while still retaining direct supply of Nestlé Australia products.
- 5.37 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.
- 5.38 Despite the lengths ALDI had gone to in order to differentiate the products, Nestlé Australia required further actions 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 unlikely to be acceptable to any retailer.

- 5.39 Nestlé Australia disagrees. It argues that evidence of customer complaints ought to conclude the matter in its favour. It relies on instances of actual customer confusion communicated to it by members of the public.
- 5.40 In all, Nestlé Australia's submissions have identified fourteen complaints over a seven month period. Nestlé Australia argues that it is generally accepted that those who make the effort to complain are typically only a small percentage of those who are dissatisfied with a product.
- 5.41 It is important, however, to look at the timing and nature of the customer contacts received by Nestlé Australia. The first customer contact received by Nestlé Australia, at least as identified in documents provided, was on 23 November 2005, some weeks after the supply of imported Nescafé instant coffee brands commenced and the same day on which Nestlé Australia resolved to lodge the notification.
- 5.42 Nestlé Australia documents reveal that by 16 January 2006, some ten weeks following the commencement of supply and six weeks after the notification had been lodged, Nestlé Australia had identified four or five consumer contacts on the issue. As noted above, by the end of June 2006, some seven months after lodging the notification, fourteen contacts have been drawn to the ACCC's attention.
- 5.43 It is important to note that many of the contacts were not confused as to the nature of the products. Some were aware that the products were imported while others noted the differentiation undertaken by ALDI and the money back offer it provided. The majority of the contacts related to concern over the taste of the product.
- 5.44 Aldi submitted it had not received any complaints on the issue.
- 5.45 The ACCC does not suggest that a small number of contacts should somehow be ignored. It does however give some idea as to the extent of the problem and the actions one might expect to be employed to resolve it. The ACCC does not consider that the differentiation requirements made by Nestlé Australia under threat of withdrawal of supply were a normal or reasonable commercial approach.
- 5.46 The Nestlé Australia documents reveal other activities being undertaken to respond to ALDI's parallel imports. Nestlé Australia staff began to prepare an extensive advertising and promotional campaign for Nescafé Blend 43 including money back offers and promotions based on the unique taste.
- 5.47 Even in this arena, however, attention was at times focused not on promoting the benefits of Nescafé Blend 43 or ensuring consumers were aware of product differences, but on avoiding customers' acquisition of the imported product. A creative brief addressed to an advertising agency on 15 November 2005, stated an objective of the advertising and promotional campaign was: "[t]o aid in the prevention of current Nescafé Blend 43 consumers from trialling parallel imports, now and in the future". This theme was repeated in other documents.

5.48 Following the ACCC Draft Notice, Nestlé Australia submitted that some ALDI stores failed to display the ALDI posters, or that poor advice was given to customers about the nature of the imported Nescafé instant coffee brands. This would understandably be of some concern, but is not addressed through the notified conduct.

Threat of competition

5.49 As noted already, having regard to the internal Nestlé Australia documents, the ACCC considers that a substantial purpose of the notified conduct was to deter ALDI from continuing to supply imported Nescafé instant coffee brands 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 grocery retailers would seek to supply imported instant coffee products (as Nestlé Australia believed such retailers were considering) in competition with ALDI.

Both of which would place downward pressure on the prices of Nestlé Australia instant coffee products and on its profits.

5.50 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 grocery retailers generating a significant competitive threat to Nestlé Australia instant coffee products.

5.51 These documents further identify that Nestlé Australia sought options to limit ALDI's ability to import these products or otherwise to cease Nestlé Australia's supply of products to ALDI.

5.52 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 grocery 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 grocery retailers as strong discipline by Nestlé Australia.

5.53 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*¹⁰ 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

¹⁰ *Universal Music Australia Pty Ltd v Australian Competition & Consumer Commission* (2003) 201 ALR 636

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”.¹¹

- 5.54 The ACCC considers that Nestlé Australia sought to ‘nip in the bud’ the emerging competition arising from ALDI’s supply of imported Nescafé instant coffee brands.
- 5.55 Nestlé Australia does not agree with the ACCC’s assessment in this regard and challenges the ACCC’s interpretation of the documents. Nestlé Australia disagrees with the relevance of the *Universal* decision and argues that it was in no position to threaten the likes of Coles and Woolworths.
- 5.56 Dealing with the relevance of the *Universal* decision, Nestlé Australia argues that *Universal Music* is not applicable to this notification due to differences in the specifics of the matters.¹²
- 5.57 The ACCC refers to the case for its statements of general principle that parallel imports can be a source of vigorous competition that threaten the profitability of local suppliers. Those suppliers can respond with vigorous efforts to compete against the parallel imports, or they can try to eliminate the new source of competition. Early action to remove the competition before it has a chance to establish itself as a force in the market can substantially lessen competition.
- 5.58 Nestlé Australia has also argued that ALDI’s total volume of sales are so small that the loss of them could not be a substantial lessening of competition.
- 5.59 While the precise figures have been excluded from the public register, they are not large in relative terms, comprising less than \$5 million per annum. The passage from *Universal Music*, and the reference in it to *Rural Press*, indicates that swift action to eliminate a source of competition before it achieves significant scale can constitute a substantial lessening of competition, even if the competitive outcomes have not yet manifested themselves fully at the time they are removed.
- 5.60 The ACCC does not rely on the volume of ALDI trade that motivated Nestlé Australia but rather the very real prospect that larger grocery retailers would follow suit causing significant damage to Nestlé Australia profits.

¹¹ Ibid, at 695

¹² 2 June 2006 submission, p 11

- 5.61 The ACCC considers the principle of the seriousness of “nipping competition in the bud” beyond the immediate volume of trade at stake is directly relevant to the current matter.
- 5.62 Nestlé Australia claims that the arguments made by the ACCC regarding Nestlé Australia’s purpose being to deter ALDI from parallel imports is the ACCC’s own theory and is without factual foundation.¹³ The ACCC maintains its arguments having close regard to internal Nestlé Australia documents.
- 5.63 Internal Nestlé Australia documents reveal that in an email dated 8 November 2005 from a senior Nestlé Australia employee to other Nestlé Australia executives in the context of drafting correspondence to Nestlé Singapore regarding ALDI’s imports, the employee proposed the following words:
- “We request your assistance to understand where this stock is being sourced from and the pricing structure that makes this product so attractive.”... “As you could well understanding [sic] this issue is causing local market instability.”
- 5.64 In a power point presentation of 11 November 2005 Nestlé Australia states the concern that:
- “Other retailers may
- Assume their shoppers will be attracted to the price point, regardless of product differences
- Choose to enter a similar Parallel import arrangement”.
- 5.65 In writing to Nestlé Singapore on 16 November 2005, another senior Nestlé Australia employee stated:
- “Aldi are not a big customer foe [sic] Nescafe and we are looking at how we might tackle the issue locally for them. Of greater concern is that the 2 major customers Woolworths and Coles who represent [REDACTED] of the grocery trade are now looking at import potential and we have been told that the ... [grocery retailer’s] team have already had some discussions with a potential supplier in Singapore on the viability of importing coffee into Australia. They are saying that this is only being considered as a response to the [sic] Aldi at this time but obviously if there is money in it, they could be tempted to proceed.”
- ...
- “Nescafe business in Oceania is a major contributor to profitability so we need to do all we can to avoid any potential impact on brand value and EBITA.”
- 5.66 In an email from a senior Nestlé Australia employee to Nestlé Singapore on 16 November 2005, the employee states:

¹³ 2 June submission, p 4

“Please don’t take my email to mean that I am blaming Nestle Singapore for this problem. I am only trying to understand how it might occur and if the pricing available would give the retailers here an opportunity to pressure us on local pricing”.

- 5.67 Nestlé Australia was clearly concerned that Aldi’s supply of imported Nescafe instant coffee products would generate competitive responses from larger grocery retailers, not just in terms of competitive importation of product but also by placing pressure on Nestlé Australia to reduce the margins on its products to make them more price competitive with the imports.
- 5.68 In its draft notice, the ACCC argued that the notified conduct was also intended to signal to other grocery retailers that might consider the importation of Nescafé instant coffee products. The ACCC argued that in this respect, the refusal to supply Nestlé Australia’s full range of products including flagship retail brands of Nescafe Blend 43 and Milo is likely to be seen by other grocery retailers as strong discipline by Nestlé Australia.
- 5.69 In its various submissions, Nestlé Australia has disagreed with the ACCC’s arguments as to signalling. They claim that the documents available to the ACCC do not support such and that it was not possible for Nestlé Australia to threaten the likes of Coles and Woolworths.
- 5.70 The ACCC has explained its view to Nestlé Australia that Nestlé Australia could signal to grocery retailers in two ways. Each can apply at the same time to different audiences.
- 5.71 The first form of signalling is a message to larger grocery retailers that they do not need to respond to the new source of competition by lowering prices or obtaining imports themselves, because Nestlé Australia was taking strong action to eliminate the problem.
- 5.72 In the second form of signalling, the withdrawal of supply to ALDI conveyed a threat to smaller grocery retailers that they should not obtain imports, because Nestlé Australia might respond by withdrawing supply of its products to them as well.
- 5.73 Again, internal Nestlé Australia documents are helpful in considering this issue. On 9 November 2005, an internal email from a senior sales executive explained that he and the Managing Director of Nestlé Australia would meet the Chief Executive Officer of one of the major grocery retailers to cover issues including the recent parallel imports of Nescafé from Singapore. In preparation for the meeting, the Nestlé Australia employee sought an understanding from colleagues on its position on matters including:
- “Trading agreements with Aldi for beverages and total business, what are our options regarding discontinuing rebates, stopping account due to outstanding payment claims etc...” ... “What else can we do to cease trading with them. What has been the response from Singapore”.
- 5.74 Nestlé Australia advises that this meeting did not proceed.

5.75 A subsequent brief for a planned meeting with the same grocery retailer in late December 2005 indicates that Nestlé Australia would explain issues surrounding the recent incidence of parallel imports. One of Nestlé Australia’s key outcomes from the meeting as set out in the brief was to:

“Gain support of ... [grocery retailer] to the importance of Nescafé B43 in the Australian market in the threat of parallel imported product. Agree to work together on B43 campaign to strengthen the brand in key areas of the marketplace and not look to import similar or other Nescafé product.”

5.76 The ACCC takes the view that all of these documents provide a strong factual basis for concluding that the withdrawal of all Nestlé Australia products from ALDI would provide signals to other grocery retailers in either of the two ways described. The ACCC maintains that its description of the notified conduct as “strong discipline” is apt.

Stopping imports

5.77 In its draft notice, the ACCC noted internal Nestlé Australia documents supported the view that it sought advice as to the ability to limit ALDI’s importation of Nestlé instant coffee brands, including efforts with Nestlé Singapore to locate the source of the imports.

5.78 The actions Nestlé Australia may have taken to restrict the physical supply of imported Nescafé instant coffee products to ALDI through discussions with Nestlé Singapore are ancillary to the notified conduct.

5.79 They demonstrate, however, a driving force within Nestlé Australia to restrict the supply of imported Nescafé instant coffee brands to Aldi through a number of means. It is directly relevant to what the ACCC considers was the primary motivation behind its notified conduct as discussed above.

5.80 Nestlé Australia has referred, in its submissions, to the practical impossibility of stopping imports. It argues it could never have succeeded in stopping the imports, so there would have been no point in ever attempting to do this and accordingly it did not.

5.81 This position is inconsistent with the internal Nestlé Australia documents. The internal documents indicate that Nestlé Australia certainly wanted to stop the imports with the assistance of Nestlé Singapore.

5.82 An undated PowerPoint presentation titled “Aldi Parallel imported Nescafé” notes as its first point under the heading “Next Steps”:

- “Letter to market head Singapore to stop supply.”

5.83 The emails from mid-November 2005 described earlier start a chain of correspondence between various Nestlé Australia and Nestlé Singapore staff, in which Nestlé Australia sought to identify ALDI’s source of supply and made enquiries as to restrictions that could be placed on that supply.

The board decision

- 5.91 Nestlé Australia has also claimed that, even if it was initially concerned about the competitive effect of the parallel imports, by the time the Board passed a resolution proposing to lodge the notification, and the notification had been lodged, attitudes within the company had undergone a transformation. It argues that its sole purpose by that time for lodging the notification was to avoid customer confusion.
- 5.92 The ACCC notes that one member of the Board was engaging in correspondence with Nestlé Singapore relating to the adverse effects on profitability, and trying to identify ALDI's supply paths and exploring opportunities to limit or restrict those paths, one week before this resolution was passed.
- 5.93 The fact that one executive and board member was receiving reports about six days after the resolution was passed relating to attempts to find ALDI's sources and prices from Singapore also does not support Nestlé Australia's position. Ongoing discussions with Nestlé Singapore on these issues almost two weeks after the notification was lodged, is inconsistent with Nestlé Australia's assertions that it knew it could not stop the imports and was only concerned to avoid customer confusion.

Conclusion on purpose

- 5.94 As has been noted already, having regard to internal documents of Nestlé Australia, 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's products; and
 - lessen the competition associated with the likelihood that other grocery retailers would seek to supply imported Nescafé instant coffee brands (as Nestlé Australia believed they were considering) in competition with ALDI.

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

- 5.95 The ACCC considers that these constitute purposes of substantially lessening competition.

Effect or likely effect of proposed conduct

- 5.96 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.
- 5.97 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.¹⁴

- 5.98 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 in which ALDI is free to advertise and sell imported Nescafé instant coffee brands while continuing to be able to receive supply of the full range of Nestlé Australia products.
- 5.99 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. This contention has been dealt with above.
- 5.100 Nestlé Australia also argued that it had merely requested reasonable differentiation of the imported Nescafé products.
- 5.101 The ACCC considers that had ALDI complied – or should it comply – with Nestlé Australia’s differentiation requirements, the marketability of the parallel imports would be significantly reduced. The large sticker which Nestlé Australia required ALDI to place over the red mug on the front of the jar, combined with the positive endorsement of Nescafé Blend 43, would discourage consumers from choosing the imported product over local products. If successful, the measures would eliminate this source of competition before other grocery retailers would feel the need to respond to it by importing similar products. The differentiation required by Nestlé Australia would to a large extent neutralise the competitive advantage of the imported Nescafé instant coffee products, so that customers would be less likely to purchase them despite their lower prices.
- 5.102 It is noteworthy that the arrival of the imports generated interest from other grocery retailers, who apparently felt the need to respond to the competitive stimulus.
- 5.103 The conduct increases the effective cost to ALDI of importing Nescafé products. Either it could import the 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 direct 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.
- 5.104 In the Draft Notice, the ACCC stated the view that these outcomes would have the effect of substantially lessening competition in the instant coffee market. Nestlé Australia submits that ALDI still sells imported Nescafé coffee and the local products of Nestlé Australia, including Nescafé Blend

¹⁴ *Dandy Power Equipment Pty Ltd v Mercury Marine Pty Ltd* (1982) 64 FLR 238, at 259 - 260

43 and Milo.¹⁵ It also notes that ALDI is free to obtain supplies of Nestlé Australia's products from third party distributors. The substance of the conduct, it argues, is merely that it refuses to supply those products directly to ALDI. On this basis, it argues that the notified conduct has not had the effect on competition anticipated by the ACCC at the time it issued the Draft Notice.

- 5.105 ALDI submits that short term effects can be ignored. Instead, the ACCC ought to consider the medium to long term effects of the conduct on its capacity to compete in the relevant markets. ALDI submits that the conduct will have a significant adverse effect on its business and its capacity to compete in the retail grocery markets in which it operates and in the market for instant coffee.
- 5.106 The ACCC considers it is possible that the notified conduct has had the effect of substantially lessening competition. It must also consider the possibility that the conduct will substantially lessen competition in the future, depending on the actions and decisions of either or both of Nestlé Australia and ALDI.
- 5.107 The ACCC must consider the possibility that Nestlé Australia's actions have deterred other grocery retailers from importing Nescafé instant coffee, which would have the effect of substantially lessening competition. In light of the documents relating to a planned meeting in late December 2005 with the CEO of a major grocery retailer, and the analysis of the signals to other smaller grocery retailers, the conduct may have had the effect of substantially lessening competition by nipping a new source of competition in the bud.
- 5.108 The ACCC understands that ALDI continues to obtain supplies of imports. However, it is noteworthy that ALDI has recently had to change the imported product from Nescafé Classic Deluxe to Nescafé Original. To the extent that ALDI is still able to sell both the imports and the local products, the effect of the conduct on competition is diminished for the time being.
- 5.109 ALDI's continuity of domestic and imported supply, however, appears to be tenuous and the additional costs involved in sourcing the products are likely to be an onerous burden. Management resources will be diverted away from the task of expanding the business towards the more elementary task of ensuring that supplies of these products are available. It is also likely that a break in the continuity of supply would have a significant effect on ALDI's capacity to compete in any of the markets relevant to this assessment of the conduct.

ALDI's scale of operations and its effect on competition

- 5.110 Nestlé Australia submits that 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.

¹⁵ 2 June 2006 submission, p 18

- 5.111 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.¹⁶
- 5.112 However, 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. The major grocery retailing chains have felt a need to respond to its presence.¹⁷
- 5.113 AC Nielsen has recently reported that ALDI's growing market share has intensified price competition amongst grocery retailing chains.¹⁸ ALDI's presence has also fuelled the development of private label ranges by their competitors.¹⁹ These factors have put pressure on growth in the grocery sector, which requires a response from grocery suppliers.²⁰ 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.²¹
- 5.114 The ACCC concludes that each ALDI store is likely to have a significant effect on price competition in the local area in which it operates. 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.

"Must-have" products

- 5.115 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 are very important to stock. Two of those products are Nescafé brand instant coffee, and preferably Nescafé Blend 43,

¹⁶ *Outboard Marine Australia Pty Ltd v Hecar Investments No 6 Pty Ltd* (1982) 44 ALR 667, at 679 - 680

¹⁷ "Feisty Aldi punches above its weight", *Australian Financial Review*, 27 July 2005

¹⁸ "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>

¹⁹ "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>

²⁰ "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,

²¹ "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>

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.

- 5.116 The importance of Nescafé Blend 43 and Milo to ALDI's business has been contested by Nestlé Australia. It claims that if ALDI can compete effectively in the retail grocery markets in which it operates without offering these products to its customers, the ACCC's views on the effect or likely effect of the notified conduct would need modification.
- 5.117 The ACCC considers 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.
- 5.118 In addition, there is evidence from other sources to support ALDI's argument that there are products which a grocery retailer should stock if it is to be viewed favourably by potential shoppers. The Office of Fair Trading in the United Kingdom has recently noted the existence of "must-have" brands and goods for retailers. It describes these products in the following terms:
- "... retailers need to stock a certain brand to be seen to be credible (e.g: allowing them to offer the 'full range') or because they bring in extra footfall. This may give rise to a minimum requirement, e.g: because the retailer would not wish to alienate customers by having run out of stock. A further example is where a certain group of final customers have a strong preference for a particular brand. Where the retailer can identify these customers, its derived demand for the product would be highly inelastic over the range of units required to meet the demand from this group of customers".²²
- 5.119 Goldberg J, in *ACCC v Australian Safeway Stores Pty Ltd (No 2)*,²³ referred to a group of "communicable" products, of which coffee was one. His Honour said of this group of products:
- "The significance of communicable products is that consumers tend to remember their prices and use the products to evaluate the comparative prices of different retailers. Accordingly, it is important for a retailer to give customers the impression that the retailer is quite competitive with respect to communicable products. Put shortly, the price of a communicable product sends a signal into the marketplace as to the general level of pricing in a supermarket and as to its competitiveness".²⁴
- 5.120 Internal Nestlé Australia documents indicate that it believed that shoppers would swap stores before swapping products. Nestlé Australia was also

²² *Selective price cuts and fidelity rebates Economic discussion paper OFT804* (Office of Fair Trading, July 2005), p 118

²³ *Australian Competition & Consumer Commission v Australian Safeway Stores Pty Ltd (No 2)* (2002) ATPR 46-215

²⁴ *Ibid*, at 53-336

keen to emphasise this point to grocery retailers, including ALDI, before this dispute arose.

- 5.121 ALDI provided retailer advertising supporting the view that Nescafé Blend 43 may be a communicable product. The ACCC understands that major grocery retailers regularly discount Nescafé Blend 43 and feature it prominently in their advertising, presumably to attract customers to their stores to buy not just Nescafé Blend 43, but all of their groceries. This reinforces the importance of Nescafé Blend 43 to grocery retailers.
- 5.122 The ACCC takes the view that there is a sufficient foundation to support the view that there are products which are very important for a grocery retailer to stock in order to compete in a retail grocery market.
- 5.123 Nestlé Australia has suggested that the conduct does not affect ALDI's capacity to compete, as the limited range of products offered by ALDI means that shoppers have to visit other grocery retailers anyway for the products ALDI does not offer. It argues that shoppers can continue to buy other products from ALDI and purchase Nescafé Blend 43 and Milo at alternative grocery retailers. The submission suggests that the conduct will produce little effect for consumers or for ALDI.
- 5.124 However, the ACCC understands it is ALDI's goal to be a "one stop" grocery retailer covering the full range of core grocery products, albeit without offering the brand diversity of other grocery retailers.
- 5.125 Conversely, because ALDI stocks a much smaller range of products than other grocery retailers, it is arguable that the continued presence of each of those products in an ALDI store becomes more important to the customers' decision to shop at ALDI. Given that many shoppers are "time poor", the removal of key products from ALDI's offering, while still available at the other grocery retailers visited by the shoppers, will reach a point at which shoppers re-evaluate the value of visiting an ALDI store. The shopper may then shift allegiance entirely to the other outlet, even if other key products are more expensive at the other outlet.

Conclusion on effect

- 5.126 The ACCC considers that the notified conduct has had the effect or is likely to have the effect of substantially lessening competition in relevant retail grocery markets and the instant coffee market for the following reasons:
- ALDI's supply of imported Nescafé instant coffee brands was introducing a significant competitive tension in those markets.
 - The notified conduct was likely to reduce that competitive tension by increasing ALDI's costs in supplying imports; and/or by reducing the consumer attractiveness of the imported products; and/or by deterring or reducing the likelihood of competitive importation or response by other retailers.
 - Such impact is greater than the direct area of trade affected having regard to ALDI's influence on competition in the retail markets; the

importance of Nescafé instant coffee products and other Nestlé products such as Milo; and the termination of emerging areas of competition.

- While ALDI’s ability to continue to source Nestlé Australia products from third parties while continuing to import Nescafé instant coffee brands has mitigated any effect, these supply arrangements are tenuous and unlikely to constrain the impact of the notified conduct in the medium to long term.

5.127 The ACCC considers the anti-competitive detriments of the conduct to be substantial.

Public benefits

5.128 Section 93 of the Act requires the ACCC to consider the public benefits produced by notified conduct.

5.129 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.

Nestlé Australia has recently also submitted that the notification “promotes Australian choices, tastes, local employment and benefits the Australian community”. It notes that consumer confusion could reduce the extent and variety of products that Nestlé Australia is prepared to offer Australians.

5.130 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.

5.131 Having regard, however, to the extent to which ALDI had independently taken steps to differentiate the imported Nescafé instant coffee products from Nestlé Australia’s products, the ACCC is of the view that Nestlé Australia’s 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 differentiation requirements that Nestlé Australia sought to impose on ALDI.

5.132 Nestlé Australia has placed great emphasis on the size and placement of stickers on products as a measure to ensure adequate product differentiation.

Case law has been cited on this point.²⁵ Nestlé Australia appears to be concerned that consumers will see a red mug on the label and assume it is Blend 43.

- 5.133 However, Nestlé Australia's own use of the same packaging device (the red mug) on another local product (Nescafé Decaf) detracts from this argument.
- 5.134 While the avoidance of customer confusion is a public benefit, ALDI was selling genuine Nescafé products manufactured by a Nestlé subsidiary, and was representing them as such. It informed consumers that the products were imports and differed from other products manufactured by a local member of the same corporate group. The ACCC considers that ALDI has taken adequate measures to differentiate the imported products from Nescafé Blend 43. Few complaints have been made by consumers, and a number of those were not that consumers had been misled regarding the origin of the product, they just didn't like the taste. It follows that the notified conduct would not produce any substantial, additional benefit from avoiding customer confusion.
- 5.135 Nestlé Australia has referred to instances in which some elements of the differentiation scheme devised by ALDI have not been complied with by individual stores.²⁶ Instances of individual non-compliance with the regime are a cause of concern, but would not be addressed by the replacement of ALDI's differentiation regime with Nestlé Australia's regime.
- 5.136 In addition, Nestlé Australia has noted that it employs about 300 people at its plant in rural Queensland. The ACCC assumes that Nestlé Australia is intimating that some or all of these jobs may be at risk if ALDI continues to import Nescafé instant coffee. The maintenance of existing employment is a public benefit. However, Nestlé Australia has not substantiated these claims. As a result, it is difficult to attach much weight to this benefit.
- 5.137 The ACCC concludes that the notified conduct generates little public benefit.

Balance of Public Benefits and Detriments

- 5.138 The public benefits and the anti-competitive detriments of notified conduct must be weighed. The ACCC considers that the notified conduct generates little public benefit. Conversely, the anti-competitive detriments are substantial. It follows that the anti-competitive detriments outweigh any public benefits produced by the notified conduct.

²⁵ 2 June 2006, submission, p 16

²⁶ 2 June 2006 submission, pp 12 - 15

6 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 that 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 grocery retailers who might respond to ALDI's sale of the imported Nescafé coffee brands by discounting Nescafé Blend 43 or by importing the same or similar products.

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

6.3 The ACCC considers that the notified conduct has had the effect or will have the likely effect of substantially lessening competition in relevant retail grocery markets and the instant coffee market for the following reasons:

- ALDI's supply of imported Nescafé instant coffee brands was introducing a significant competitive tension in those markets.
- The notified conduct was likely to reduce that competitive tension by increasing ALDI's costs in supplying imports; and/or by reducing the consumer attractiveness of the imported products; and/or by deterring or reducing the likelihood of competitive importation or response by other retailers.
- Such impact is greater than the direct area of trade affected having regard to ALDI's influence on competition in the retail markets; the importance on Nescafé instant coffee products and other Nestlé products such as Milo; and the termination of emerging areas of competition.
- While ALDI's ability to continue to source Nestlé Australia products from third parties while continuing to import Nescafé instant coffee brands has mitigated any effect, these supply arrangements are tenuous and unlikely to constrain the impact of the notified conduct in the medium to long term.

6.4 The ACCC considers the anti-competitive detriments of the conduct to be substantial.

- 6.5 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 substantial public benefits resulting from the conduct.
- 6.6 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.
- 6.7 Accordingly, the ACCC issues this notice to revoke the notification lodged by Nestlé Australia on 2 December 2005.