

# HONDA

Honda Australia Motorcycle & Power Equipment Pty. Ltd.  
ABN 96 006 662 862

1954-1956 Sydney Road, Campbellfield, VIC 3081  
Private Bag No 19 Somerton, VIC 3062  
Ph: (03) 9270 1111  
Fax: (03) 9270 1133 (Admin) Fax: (03) 9270 1122 (Sales)  
www.hondampe.com.au

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Australian Competition & Consumer Commission  
23 Marcus Clarke Street  
Canberra ACT 2601

**Attention:** Dr Richard Chadwick/Ms Monica Bourke  
Adjudication Branch

Dear Dr Chadwick and Ms Bourke,

**Submission regarding Exclusive Dealing Notification N93925 lodged by Marine Power International Pty Ltd**

I refer to your letter dated 14 April 2009 inviting Honda Australia Motorcycle and Power Equipment Pty Ltd (Honda MPE) to make a submission on the likely public benefits and effect on competition, or any other public detriment, from the arrangements proposed by Marine Power International Pty Ltd (Marine Power) in its exclusive dealing notification lodged on 23 March 2009 (Notification). Thank you for providing Honda MPE with the opportunity to make a submission in relation to the Notification.

Please note that Honda MPE claims confidentiality in respect of components of this letter, as highlighted below.

1. **Executive summary**

The ACCC should revoke Marine Power's Notification. The exclusive dealing conduct which is notified involves dealers entering into agreements (**Exclusive Dealer Agreements**) under which the dealers (**Exclusive Mercury Dealers**) agree to stock Mercury outboard engines exclusively. It involves them agreeing not to acquire, except to a limited extent, outboard marine engines sold by distributors such as Honda MPE (referred to in your letter as "suppliers"), who are competitors of Marine Power. The exclusive dealing conduct will have the likely effect of substantially lessening competition and, in all the circumstances, the benefit to the public from the conduct, if any, will not outweigh the detriment to the public caused by the lessening of competition from the conduct.

Honda MPE has a number of concerns about the likely effect of the conduct described in the Notification. In summary, Honda MPE's concerns are:

- (1) The relevant markets are not fully competitive even without the notified conduct. With the notified conduct they will become substantially less competitive.
- (2) The notified conduct will result in a further reduction in the ability of distributors to compete in wholesale markets and will significantly reduce the choice of outboard engines available to consumers in retail markets.
- (3) The notified conduct will be implemented selectively at Marine Power's discretion in areas that Marine Power determines there is "retail competition from other boat and engine resellers" and where "sales of its Mercury Outboards would benefit from distribution through a specialist Mercury reseller". This conduct cannot be regulated and competitors and the ACCC cannot be certain that the areas in which the Exclusive Dealer Agreements are to be implemented are areas where sufficient competition exists to overcome the anti-competitive effects of the tying arrangements, if indeed any such areas exist.

## 2. Confidentiality

Honda MPE claims confidentiality over certain parts of this submission on the grounds that they contain details of Honda MPE's customer base, market share, production output and/or pricing, in each case comprising information which is commercially sensitive to Honda MPE.

## 3. Marine equipment industry

### 3.1 Background and structure

Like Marine Power, Honda MPE distributes outboard engines to a network of independent marine equipment dealers. Distributors are almost entirely dependent on these dealers for sales. As the industry currently operates, the dealers generally stock a number of different brands of boats and outboard engines, and their most significant source of revenue is the sale of boat packages to consumers. A boat package will typically comprise a boat, engine and trailer combination.

#### [Restriction of publication claimed]

As set out in the Notification, the majority of outboard engines are sold either as part of these packages or as "repower" units. Consumers have some ability to choose the brand of engine they would like fitted to the boat, but there are constraints on their exercise of this choice as described below.

The outboard engine industry is not particularly profitable and has been significantly impacted by the current poor economic conditions, as consumer spending in the industry is mostly discretionary. The Outboard Engine Distributor Association (OEDA) estimates that there has been a [Restriction of publication claimed] in unit sales in the period from 1 January 2009 to 31 March 2009 as compared to the same period last year<sup>1</sup>. Further, according to Honda MPE's own records, in the past 12 to 15 months, [Restriction of publication claimed] marine equipment dealerships (approx [Restriction of publication claimed] of all dealerships nationally) have closed. Honda MPE anticipates that the current economic climate will accelerate the rationalisation amongst dealers that has been occurring for some years. Honda MPE submits that low profitability and industry rationalisation result in medium to high barriers to entry into the market at both the distributor and dealer level.

The marine equipment industry operates in a fragmented market. There are many models of boats available. There are a large number of boat builders, and many boat builders have up to 10 to 20 models each.

There are few dealers who sell engines exclusively. The largest distributors of outboard engines ([Restriction of publication claimed]) have both the greatest geographic penetration (i.e. more dealers more widely spread) and better access to larger dealers than their smaller counterparts ([Restriction of publication claimed]).

Dealers sell in regional markets. It is necessary that a region have a population of some substance to support a dealership. It follows, therefore, that not all towns have a dealer. Honda MPE estimates that a population of approximately [Restriction of publication claimed] is required to support multiple dealers.

Honda MPE expects that the boat engine industry will be significantly impacted by the introduction of environmental emissions standards by the Department of the Environment, Water, Heritage and the Arts (DEWHA) within the next 2 to 3 years. It is expected that the emissions standards will only apply to new engines sold and not to engines sold prior to the introduction date. There are three main types of outboard boat engine which are: 2-stroke

<sup>1</sup> [Restriction of publication claimed].

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carburettor, 2-stroke direct fuel injection (2-stroke DFI) and 4-stroke. The 2-stroke DFI and 4-stroke are more environmentally friendly than the high polluting, older technology 2-stroke carburettor models. It is expected that the emissions standards will result in restricting the sale of 2-stroke carburettor engines in line with developed markets in USA and Europe.

### 3.2 Engine manufacturers and distributors

The six brands that are members of OEDA account for [Restriction of publication claimed] of all outboard engines sold in Australia. Based on figures collected by ERG International for OEDA<sup>2</sup>, the approximate national market share held by these brands in total and per type of engine for calendar year 2008 is<sup>3</sup>:

#### [Restriction of publication claimed]

While national market share provides an informative overview of the market positions of the distributors nationally it is more relevant to analyse capital city/regional market shares when considering impacts on competition because it is in these areas that dealers are in competition. Honda MPE submits that this has been conceded by Marine Power in its Notification by stating that it will not appoint Exclusive Mercury Dealers in less populated areas.

As noted above, 2-stroke DFI and 4-stroke are more environmentally friendly than 2-stroke carburettor engines. The introduction of emissions standards within the next 2 to 3 years will therefore negatively affect the major producers/market share holders of the 2-stroke carburettor engines ([Restriction of publication claimed]) more significantly than the other distributors.

Outboard engines generally have a lifespan of between [Restriction of publication claimed] and are mostly used for trailer boats. As such, outboard engines do not generally compete directly with inboard engines. The only area where there is some competition between outboard and inboard engines is for ski boats which is a relatively small component of the wider boat engine market.

#### [Restriction of publication claimed]

### 3.3 Boat manufacturers

There are two main types of boats that are suited to outboard engine use – aluminium and fibreglass. The major manufacturer of aluminium boats is Telwater which manufactures and distributes the brands Quintrex, Stacer and Savage. Savage was previously owned by Marine Power and was sold to Telwater in 2008. [Restriction of publication claimed]

There are three main manufacturers of fibreglass boats. They are Haines Signature, Haines Hunter (no relationship with Haines Signature) and CruiseCraft. All boat manufacturers provide floor financing to dealers in the same way that engine manufacturers do.

### 3.4 Dealers

Honda MPE estimates that there are between [Restriction of publication claimed] dealers of outboard engines nationally that could form part of a "sales network" for a distributor. Other dealers exist but these are likely to be service only dealers or very small dealers. Generally, dealers stock between [Restriction of publication claimed] boat brands. There are very few dealers who only stock one brand of boat. Annual turnover per

<sup>2</sup> [Restriction of publication claimed].

<sup>3</sup> [Restriction of publication claimed].

dealership is between **[Restriction of publication claimed]** and consolidation of dealers is occurring in the market as discussed above.

Dealers' main source of revenue is to sell bundled boat, engine and trailer packages. There is low transparency of the cost of the bundled components and dealers tend to up-sell from basic packages. Engines are, to a high degree, interchangeable or substitutable **[Restriction of publication claimed]**. Subject to the specifications of the boat or engine (i.e. the size of the boat or the horse power of the engine) most boats and engines are compatible with each other. This means that packages are mostly only restricted by the extent of brands stocked by the dealer. However, dealers do not tend to emphasise the substitutability of engines. Point of sale material (**POS material**) is often specific to particular brands. For example, all Telwater POS material specifies Mercury, even though other engines are generally substitutable.

"Repower" is also an important aspect of the industry and has become more important in the current economic climate as there has been a noted decrease in the replacement of boats and engines. "Repowering" is the process of upgrading a tired or older technology engine with a new engine. Honda MPE estimates that at present approximately **[Restriction of publication claimed]** of all engines sold are for repower.

As is recognised by the Notification, a dealer's business is not restricted to the resupply of marine equipment to consumers. It includes after sales repairs, maintenance and servicing. Dealers are generally restricted to servicing the brands of engine which they sell. This is because engine parts are not interchangeable and genuine parts are not generally available to general servicing dealers – only to dealers which supply that particular brand. For example, a dealer who does not resupply Honda engines will not generally be able to service Honda engines as they would not have access to Honda parts. Boat owners need to visit dealers 2 to 3 times per year for servicing and maintenance of their engine and boat. This requirement for regular visitation means that boat owners prefer to develop a relationship with their dealer and this is a motivating factor in acquiring their boat locally rather than basing the purchase purely on price.

### 3.5 Customers

A high proportion of boats, and therefore outboard engines, are used for recreational purposes, and sales are thus discretionary. Honda MPE estimates that **[Restriction of publication claimed]** of engine sales are for recreational purposes, with the remainder being for commercial purposes.

Customers are faced with high running costs associated with the products they buy. These running costs (excluding fuel) are approximately **[Restriction of publication claimed]** of the initial purchase price per annum. The costs include boat and trailer registration, servicing and repairs.

While customers will travel to seek out the best or better buy, there is a preference to buy locally and develop a relationship with their dealer because they will have to visit their dealer frequently for servicing and maintenance. This is described in the outboard engine industry as the concept of "visit frequency".

There is little transparency in pricing in the market. As outlined above, generally engines are sold as part of a package which will include boat, engine and trailer. The package is sold for a package price and a break down of the price of each component is generally not provided. This lack of transparency means that the customer is not aware of the potential price differential between varying engines. Further, engine manufacturers do not generally publicise recommended retail prices (**RRP**) although dealers are provided with them and point of sale material provided to customers does not set out the price of engines.

#### 4. Relevant markets

##### 4.1 Market definition

We note that Marine Power has defined the relevant markets as the:

- (1) Wholesale market for boat engines and parts and accessories in Australia (**Wholesale Market**); and
- (2) Retail market in Australia for powerboats, boat engines and related parts and accessories and servicing and repairs (**Retail Market**).

It is Honda MPE's view that such a definition is insufficient. While Marine Power identifies national markets, in its Notification it acknowledges that competition between dealers is stronger in some locations than others. As a market is the "area of close competition between firms" or the "field of rivalry between them" we consider that the relevant markets in which the effect on competition must be measured are the smaller regional markets for boat engines, parts and accessories.<sup>4</sup> It may be that there is a national market for manufacturers and distributors as they compete nationally but this is not the case for the retail aspect of the outboard engine industry. It is clear that a dealer in Melbourne is not in competition with one in Sydney, and a dealer on the NSW North Coast does not compete with dealers in Sydney.

This submission makes reference to the likely effects of the conduct in these other regional markets.

##### 4.2 Barriers to entry

Honda MPE submits that there are medium to high barriers to entry into the retail boat engine market which restrict the ability for resupply substitution to occur at the retail level. This means that any lessening of competition cannot easily be alleviated by new entrants to the retail market. These barriers to entry are mostly economic and have been heightened by the current economic conditions.

As outlined above, the outboard engine industry (and the boat industry generally) is not particularly profitable for manufacturers and dealers alike. In the past 12 to 15 months [Restriction of publication claimed] dealerships (approx [Restriction of publication claimed] of all dealerships nationally) have closed. In such a market it is unlikely that new dealers will enter the market to alleviate the lessening of competition created by the notified conduct.

The market relies on the discretionary spending of its consumers. As the economic climate has worsened, discretionary spending has turned away from boats and boat engines. This is evidenced by the [Restriction of publication claimed] in unit sales outlined above and accelerated consolidation of dealerships. As a mostly non-essential, recreational product, a buoyant economy is necessary to drive the market. The current economic climate has significantly reduced returns available the market. This creates barriers to entry and it is likely, Honda MPE submits, that these barriers to entry will remain, to some extent, for the life of the Exclusive Dealer Agreements (3 years).

<sup>4</sup> *Re Queensland Co-operative Milling Association Ltd; Re Defiance Holdings Ltd (1976) 25 FLR 169 at 190.*

**5. Effect of the notified conduct**

**5.1 Competition**

Ability to regulate Notification

Marine Power states in its Notification that the Exclusive Dealer Agreement will "generally be offered to selected Mercury dealers or prospective Mercury dealers based in populated regions in which there exists retail competition from other boat and engine resellers and in which areas Marine Power International believes that sales of its Mercury Outboards would benefit from distribution through a specialist Mercury reseller".

Honda MPE is concerned with this statement for two reasons:

- (1) Marine Power has not proposed how it will define such locations, essentially meaning any area could be selected; and
- (2) Without any process for selection of the areas provided by Marine Power, the ACCC may not be able to regulate the notified conduct to ensure that Marine Power does not offer Exclusive Dealer Agreements in areas that are not populated or where there does not exist retail competition.

For these reasons it is Honda MPE's view that the notified conduct will not be able to be adequately regulated and that the Notification should be revoked.

Lessening of competition

Mercury presently has a large market share nationally and regionally and it has a high penetration both geographically and to quality dealers. This status will mean that dealers who are approached to become Exclusive Mercury Dealers will be pressured to become so. This will lead to a decrease in interbrand competition both "in-dealer" and between dealers.

The creation of Exclusive Mercury Dealers will work to lessen competition in the smaller regional markets as it will reduce competition between brands within a dealership. Whereas previously a customer may have had the choice to purchase an outboard engine out of a number of different engines stocked by the dealer to put on their boat, the notified conduct will result in the limitation of this choice. Such limitation of choice combined with restricted resupply substitution and small regional markets will lead to a diminution in the independent price rivalry of outboard engines and a lessening of competition in the markets.

It is Honda MPE's view that there will be a reduction in interbrand competition in areas where Exclusive Dealer Agreements are entered into because rival manufacturers will be prevented from selling to Exclusive Mercury Dealers. Accordingly, distributors and manufacturers of outboard engines will be squeezed out of these areas.

**[Restriction of publication claimed]**

The notified conduct will have a greater negative impact on brands with a smaller market share such as [Restriction of publication claimed]. [Restriction of publication claimed]

Finally, because of the lessening of competition, sole manufacturer dealers will have lower negotiating power in relation to floor plan financing. This could lead to an increase in cost for the dealer which may be passed on to the consumer.

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## 5.2 Public Detriments

As well as lessening competition in the regional markets, it is Honda MPE's view that there will be significant public detriment arising from the notified conduct. This public detriment will impact both consumers and dealers and there are potential environmental effects which could cause detriment to the public generally.

### Detriment to consumers

Should the Notification be allowed to stand, the structure of the industry will change substantially and certain dealers will move from supplying a variety of outboard engines to consumers to only supplying one type of outboard engine to consumers. This may then mean that in a particular regional market, consumers will only be able to buy a certain type of boat fitted with a Mercury engine as that Exclusive Mercury Dealer no longer supplies different types of engines.

While the Notification states that a dealer may continue to supply products that are noted in the Exclusive Dealer Agreement as being products sold by the dealer before the Exclusive Dealer Agreement came into operation, Honda MPE considers that this will not occur in practice. Given that the Exclusive Dealer Agreement will contain quarterly sales targets, dealers will have an incentive to push sales of Mercury products to consumers and accordingly, the fact that dealers may continue to supply competing products will be inconsequential.

The Exclusive Dealer Agreements will result in an alteration of the market structure in the relevant markets by limiting the number of brands of outboard engines available, so that consumers no longer have the same choice available in a geographical market as was previously available. Consumers will have reduced ability to "mix and match" to their preference. While they may, at an Exclusive Mercury Dealer, have their choice of brand of boat they will only be able to purchase a Mercury engine.

In some cases, these regional markets may only be serviced by a small number of dealers as there is not great concentration of boat dealerships in Australia generally. As noted above, consumers in this market do not travel great distances to purchase boats. A consumer will likely not leave their regional market to purchase a boat even if they would like the choice of purchasing a different outboard engine. This is bolstered by the fact that servicing and maintenance is an essential element in owning a boat engine and given the restrictions on servicing in the market outlined above, a customer is likely to choose the dealer most convenient to them so that their return for servicing and maintenance of the engine is not cumbersome.

## 5.3 Public Benefits

Honda MPE does not agree with the public benefits described in the Notification. Even if the efficiencies claimed exist, for the benefits to dealers by way of increased efficiencies outlined in the Notification to be a public benefit they need to meet the total welfare standard. It is Honda MPE's view that this standard will not be met as it is unlikely that any savings the dealer makes as a result of the notified conduct, if any, will be passed on to the consumer.<sup>5</sup>

Further, Marine Power's claims that the benefit to dealers result in public benefits are not entirely correct. While assistance to make small businesses more efficient has been recognised as a public benefit by the ACCC and the Australian Competition Tribunal previously, generally, for a benefit to be regarded as a public benefit it must be seen as a benefit to the community generally.<sup>6</sup> In Honda MPE's view, benefit to dealers alone is not a benefit to the community generally.

<sup>5</sup> *Re Qantas Airways Ltd* [2004] ACompT 9 at [91].

<sup>6</sup> *Re Queensland Independent Wholesalers Limited* (1995) ATPR 41, 438

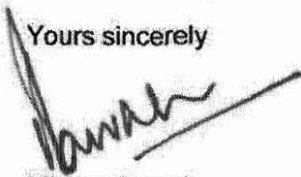
While this does not mean that private benefit or private detriment are necessarily irrelevant, as set out in *Re Rural Traders Co-Operative (WA) Limited (1979) ATPR 40-110 at 18,122 (Rural Traders)*, when a benefit or a detriment to a particular individual or segment of the public is pressed as a relevant benefit or detriment to the public, it must be assessed whether the benefit or detriment to the individual or group can properly be so categorised. The Tribunal in *Rural Traders* stated that, that assessment will ordinarily involve the consideration of whether the community generally has an interest in the individual or group being so benefited or disadvantaged and whether the benefit or detriment involves detriment or benefit to other individuals or groups. In our submission, any benefit derived by the dealers results in a significant detriment to other manufacturers and consumers.

Accordingly, Honda MPE considers that there any no public benefits that arise from the notified conduct.

We submit that the Notification should be revoked.

Please do not hesitate to contact us if you require any further information.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Vikram Pawah', is written over a horizontal line.

Vikram Pawah  
General Manager - Honda Power Equipment & Marine  
Honda Australia Motorcycles & Power Equipment P/L