

ANZARUT & HOLM

LAWYERS

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1 March 2013

Ms Imogen Hartcher-O'Brien
Director
Adjudication Branch
Australian Competition & Consumer Commission
Canberra ACT 2601

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Dear Imogen

Narta International Pty Ltd Authorisation Application A91335

I refer to the pre-decision conference held on 15 February 2013 and the Commission's invitation to provide a further written submission on matters discussed. This submission should be treated as supplemental to that provided to the Commission on 8 February 2013.

This submission addresses the following queries raised by Commission members Dr Jill Walker and Dr Michael Schaper at the pre decision conference, being:

1. Is Narta's inability to impose a MAP a decisive factor in its ability to negotiate supply of Exclusive Products?
2. Why did Narta not have the same difficulty in accessing Exclusive Products prior to now?
3. Would a MAP become the sell price?

It also responds to the 'public detriment' and 'likely future with and without' findings in the Commission's Draft Determination (Draft).

Narta's Ability to Negotiate Supply of Exclusive Products and launches of New Products

- 1) Narta understand that the Commission remains of the view that the reason that Narta is experiencing difficulty in negotiating access to these products is due to an inability to offer consistent marketing of such products across its disparate member base and not due to its inability to apply a MAP.
- 2) In this regard we understand that 'consistent marketing' (per paragraphs 54 (b)-(g) of the Draft Determination) is a reference to:
 - a. the level of marketing and advertising support to be provided by the retail group;

- b. the quality of the retail group's sales staff and the quality of the retail experience provided by the retail group to consumers;
 - c. the ability and willingness of the retail group to maintain the necessary level of stock in order to cover the supplier's projected demand;
 - d. the nature and quality of after-sales services provided by the retail group;
 - e. the convenience of billing arrangements and other costs for the supplier associated with dealing with the retail group; and
 - f. the typical consumer profile and price points serviced by the retail group.
- 3) Narta confirms that it has focussed upon providing suppliers with a 'single order book' as a priority over the last 2 years. This was recognised as a necessity to remain competitive and efficient against the large single banner retailers. The changes that Narta has implemented, including a more than \$1 million IT system upgrade, have resulted in Narta now being able to meet supplier's requirements in relation to the factors (a)-(f) listed above.
- 4) Specifically Narta provides members with:
- a. assistance to prepare advertising and catalogues in a consistent format (excluding price and branding),
 - b. placement of such advertising;
 - c. adoption of consistent point of sale displays and in store product placement;
 - d. training for member's sales staff in particular products, including specific supplier local training (a recent example being that provided in relation to the BEKO range);
 - e. assistance for members to monitor and maintain stock levels, while also giving transparency to the suppliers to assist with their planning
 - f. Adoption and implementation of a totally new IT platform for forecasting, collating and placing of orders via Narta;
 - g. a single point for ordering and payment for the supplier for all aggregated orders. By way of example 5 years ago this centralisation would not have exceeded 15% of Narta's total orders, while now up to 80% of major suppliers orders to the group are 'single book'.
- 5) In short the only element of the 'consistent marketing' requirement that Narta is unable to meet is that of a consistent advertising price.
- 6) In this regard I confirm my client's oral advice to the Commission that:
- Mr Michael Jackson for Narta was actively negotiating for supply of Exclusive Products and new technology launches. These negotiations commenced in September 2012 with supplier meetings with the Narta Board and key principals of the membership base. Subsequently further supplier meetings were held in October and November and final requests made in Las Vegas at CES (Consumer and Electronics show) in January 2013.
 - Meetings to finalise and confirm were booked and then held in February 2013 to finalise all line ups for Audio Visual. From the earlier meetings with suppliers Narta was confident of securing a number of exclusives and first or joint launch to market of identified new products.

- Shortly after publication of the Commission's Draft Determination, which was made between CES and the February meetings, Michael Jackson received calls from a number of suppliers expressing concerns with the draft outcome.
- Subsequently Narta was informed by [REDACTED]

7) We submit that the Commission must accept that Narta's inability to offer the MAP is a critical factor in a supplier deciding whether or not to supply Exclusive Product, as it is the only key 'consistent marketing' factor of those identified by the Commission in its Draft Determination upon which Narta cannot deliver, while all its competitors can.

Why was this not an issue for Narta previously?

8) The consumer electrical goods market is a highly competitive and dynamic market. In recent years it has been characterised by increasing concentration at both supplier and retailer level. In addition a number of major suppliers continue to struggle with profitability. Suppliers are now very focussed upon increasing profit levels and this is illustrated by trends such as suppliers:

- moving to 'agency' sales models; and
- seeking to increase product differentiation by offering different Exclusive Product through different retail channels.

9) Until recent years Narta enjoyed fairly generic access to product, subject to negotiation of terms. Suppliers are now however treating premium and new release product differently and focussing upon a more limited and 'exclusive' distribution model.

10) An example of this is [REDACTED]

11) This market trend has the potential to significantly damage Narta and its members, as being excluded from access to Exclusive Products is disproportionately damaging to a retailer, as the Retraction example discussed at the pre decision conference illustrates.

12) To reiterate the damage that flows for Narta members is:

- loss of consumer attention, as it becomes known that Narta member businesses do not have stock of these products, or equivalent products;
- loss of the ability to differentiate their business; and
- Loss of the ability to cross sell and up sell product across a supplier range.

13) In the television example given, [REDACTED]

Does Advertising Price Fix Sale price?

14) Consumer electrical products are in a highly competitive wholesale and retail market. It can clearly be distinguished from the retailing of groceries or apparel, where Narta

accepts the advertised price is almost always the price at which the product is actually sold. The reverse is however true in consumer electrical goods and Narta members consistent response to being asked about this is that: 'nobody pays the advertised price'.

15) In this market consumers have been educated to expect a discount. This has occurred by a combination of advertising emphasising 'Everything is negotiable' (Bing Lee); 'Pay Less Pay Cash' (the Good Guys); 'Best Price Guarantee' (Harvey Norman) and the prevalence of on-line price comparison websites and offers. Narta has accessed updated data on industry sell price versus advertising price for December 2012 as well as member specific pricing on products advertised in the December 2012 catalogues and this shows that average sell price is consistently at a discount to the advertised price. It also shows that the level of discount varied from member to member and therefore from transaction to transaction. A sample of referenced member catalogues are **Attachment 1**.

16) In addition Narta invites the Commission to have staff attend any major retailer of consumer electrical goods and ask for a 'best price' or to price match on an advertised item. Provided that item is not under an agency sales arrangement, we consider that this exercise would conclusively prove that the advertised price in this market is seldom, if ever, the actual sale price.

Public Detriments

17) The Draft concludes that two main areas of competition between electrical goods retailers will be affected:

- Intra-brand competition (that between Narta members); and
- Inter-brand competition (that between all retailers of electrical goods).

18) In Narta's submission in reaching these draft conclusions the Commission has:

- under estimated the power of market forces in the electrical goods retail market; and
- applied too narrow a market definition by assessing the public detriments in the context of 'MAP Products' in isolation of the broader product markets as identified in in paragraph 35 of the Draft.

19) In relation to both 'intra' and 'inter' brand competition the existence of a MAP does nothing to lessen the incentive an individual Narta member has to make a sale. If they do not make a sale, they receive no financial benefit and that benefit instead accrues to a competitor. Narta members, like all other retailers, are in business to make a profit and they do not make profits if they do not make sales.

20) A Narta member would only have an ability to 'give less and charge more' if the MAP product was unique, or had few substitutes. This is not the case for any electrical goods. Rather the full range of products in a particular category, irrespective of price point, will perform the same basic core function (e.g. fridges, DVD players, washing machines, stoves, televisions). Further, each supplier will have substitutable products at corresponding price points across their range. Therefore a television that has had a MAP applied will be competing against products with similar functionality offered by alternative suppliers and with generally substitutable products at different price points. In our submission the introduction of a MAP may only increase the level of discounting of MAP products, rather than necessarily 'enable retailers to earn higher margins'¹ as postulated in the Draft.

¹ Draft Determination paragraph 75(b).

- 21) In this regard a distinction can be made in relation to what has been described as 'must have' products, which can be seen as products that create a level of excitement or consumer interest, rather than being unique or without substitute in an objective economic sense. Narta retailers being able to stock such products is as important from a retail positioning perspective as it is for having the ability to actually make sales of such products. A customer may be drawn to a Narta retailer to view a new launch product that has a MAP, but may well decide to purchase a different product that is not subject to the MAP. For example Narta members not having access to 3D television for the first 3 months after launch was as damaging to Narta members because consumers interested in this technology bypassed their stores, as it was because of the loss of potential sales of this product.
- 22) Further, this is not a market that fails due to information asymmetry. To the contrary this market probably has the most amount of real time information available to consumers of any consumer market. Consumers can and do search for best prices on product on-line at home and while shopping using mobile devices. Retailers in this market segment actively promote price matching and discounting in their online, print and television advertising and consumers are generally fully aware of this potential.
- 23) In short this is a highly competitive market that will not fail due to the proposed MAP, but rather at a macro level will benefit by enabling Narta to compete on the same terms as all other major players in the wholesale market for the acquisition of electrical goods.

Interaction between bricks and mortar retailing and online retailing

- 24) Narta submits that the Commission's Draft is in error when it concludes:
- a) 'products selling prices are likely to be dependent upon the products advertising prices...[...] Currently individual Narta members advertise a particular brand or product at different prices and so their selling prices differ, despite Reference Pricing' (Draft Para 78).
 - b) a MAP will '...disadvantage online Narta retailers who do not discount from advertising prices [...] and reduce the competitive constraint that they impose on other Narta retailers.' (Para 75(c)). 'Selling prices offered through online retailers are rarely negotiated' (para 79) and '...the advertising price of goods sold by [on-line] electrical goods retailers is likely to be the same as the selling price.' (para 84);
 - c) '...online retailers are usually able to offer lower selling prices than brick and mortar retailers because their costs are lower.' (Para 79) and '...the on-line advertising price, which is often lower than the bricks and mortar advertising price, may be used as a Reference Price for sales at bricks and mortar retailers.' (Para. 80).
 - d) 'The process of quick and easy online comparison, in turn, gives consumers a point of leverage in negotiating prices with brick and mortar retailers...' (para 80)
- 25) To the contrary Narta notes:
- a) Any advertised price and/or any manufacturer's recommended retail price is likely to be a 'point of reference' in a price negotiation. There is no intrinsic evil in having such a 'point of reference' and in fact retailers advertising prices drive advertising price responses from other retailers. More importantly having a 'point of reference' does not determine an outcome of a subsequent price negotiation in an otherwise competitive market. Actual selling prices in this market demonstrably vary based upon the retailer's willingness to discount and how hard the customer negotiates. If it were otherwise every Harvey Norman or Good Guys customer would purchase the

same product at substantially the same price, being the price that results from the Commission's assumed consistent 'lump-sum discounts or percentage discounts off' the uniform advertising price that each of those retail businesses have applied to that particular product at a particular point in time. Selling prices are manifestly not 'dependant' upon the advertising price and the variance in Narta member retail prices for a product is not solely due to differing advertising prices and rather are substantially the result of the individual negotiations that have occurred.

- b) On-line sellers do discount from their advertised price and the selling price of on-line sellers is not 'likely to be the same' as the advertising price. **Attachment 1** shows that the average sell price of the single largest on-line outlet, Appliances On-Line of a selection of products advertised in its December catalogue was consistently at a discount to its advertised price. This is likely to be due to price negotiation, either on-line, through telephone contact, or due to their 'Facebook fan discounts'. While the level of discounting is less than for bricks and mortar, this is a trend we consider is likely to increase;
 - c) Importantly on-line sellers do not, on average, offer lower advertised prices for products than bricks and mortar outlets and, in addition, on-line selling prices are commonly higher than the selling price of the same products offered from bricks and mortar. This is illustrated in **Attachment 2** where the average sell price of large volume television product as reported by GFK is contrasted with CMS data showing advertised prices (both catalogue/print and on-line). This fact is at least partially why on-lines sales constitute less than 5% of total sales of electrical goods. In essence on-line sales trade on convenience and ease of sale process, rather than on aggressive discounting of advertised or selling prices.
 - d) Narta submits that the process outlined in paragraph 80 and 83 of the Draft is in fact a reverse of what is currently occurring. The lower selling prices offered by brick and mortar retailers is driving increased discounting by the on-line retailers. This in turn is likely to cause online retailers to adopt more mechanisms in order for them to differentiate their selling price from the advertised price. Alternatively they may forgo sales growth to maintain their higher margins.
- 26) More over Narta submits that the Commission is in error in placing such weight on the on-line sales portion of the retail market, given its relative size and importance in the context of the total market. On-line sales in electrical goods are merely an additional sales channel for most retailers and a supplement to their brick and mortar business, not a substitute for it. So, for example, Appliances On-Line is owned by bricks and mortar Narta member Winnings Appliances. Competition in this market is very much driven by bricks and mortar retailers, as this is where the consumer is best able to play off competing retailers to achieve the best possible deal.

The likely future with and without

- 27) Narta considers that the likely future with and without analysis at paragraphs 36-39 of the Draft Determination is deficient. We submit that the 'likely future without' the authorisation sought is as follows:

- Narta will be unable to access Exclusive Products;
- Narta members will be at a continuing and increasing competitive disadvantage to other buying group and corporate retailers;
- Those other buying groups and corporate retailers will be under reduced competitive pressure, as they will have exclusive access to key new release and innovative products which they will continue to advertise at a uniform price.

- Consumers will no longer have the bargaining power they currently enjoy and therefore prices (and retail margins) on such 'must have' products will increase.
- Narta members will be at an increased risk of failing,
- Narta will be at an increased risk of not being able to maintain its scale and ability to source product at competitive wholesale prices.
- The retail market for consumer electronics will become more concentrated and less competitive.

28) We further submit that the 'likely future with' the authorisation sought is as follows:

- Narta will be able to access Exclusive Products;
- Narta members will continue to provide direct competition to other buying groups and corporate retailers;
- Consumers bargaining power and competition in the retail market will be maintained;
- Narta will remain a viable business supporting its disparate member base, including small businesses in both metropolitan and regional Australia.

Scope of products to which a MAP Is applied

29) The Commission has expressed concerns regarding the difficulty Narta has had in precisely defining the products to which a MAP may be applied and has postulated that it could allow for 'a significant increase in scope depending upon future interpretations of these terms'.(Draft para 93).

■ In our submission this concern is unfounded. Importantly the availability of exclusive product/new release/premium product is purely a decision for the supplier. In practice suppliers are now dividing up their product range between retailers and do not commit more than a small model range exclusively to any one retail channel. ■

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31) We consider this approach will be typical for major suppliers going forward and no supplier will put more than a smaller part of its range exclusively with any one retail channel. In effect the scope of product to which Narta can impose a MAP will be self-limiting and is not something that can be significantly increased in scope at the whim of Narta. Further, even if the Commission were to grant the authorisation application it is now too late for Narta to obtain any exclusive product access for 2013, as these supply decisions were locked-in with most suppliers during February for the next 12 -18 months.

32) Once again the example of the other major buying groups, Harvey Norman and the Good Guys is instructive. Major suppliers are providing each of these businesses in 2013 with exclusive or joint access to new products on release, exclusive or joint access to some premium product and to some exclusive ranges of product within product categories. We understand that they are not providing exclusive or sole access across an entire product range (or even a substantial portion) to either of these retailers, despite their ability to apply a consistent advertising price across all products supplied.

33) We therefore remain of the view that the actual extent of application of the MAP will not exceed 2% by volume of Narta total sales. The subsequent figures provided in our submission dated 5 December 2012 were expressed to be the theoretical maximum application of the MAP if supplier's agreed to Narta's full 'wish list' of potential exclusive product. It is not a likely scenario for the scope of application of the MAP.

Conclusions

34) Narta repeats its submission of 8 February 2013 that the Draft is in error both in its finding that an ability to impose a MAP is not critical to Narta being able to access Exclusive Products and in its consequent balancing of public benefit against anti-competitive detriment. We repeat our submission that the authorisation being granted will result in significant pro-competitive public benefit and minimal public detriment.

35) In particular Narta submits that it is in the interest of maintaining the existing highly competitive market that Narta be able to compete on equivalent terms for wholesale supply of consumer electrical products. The current inequality otherwise risks further concentration of the market at both retail and wholesale level, to the ultimate detriment of Australian consumers.

36) However, if the Commission still remains uncertain of the public benefits put forward, Narta suggests that a way of mitigating the risks highlighted above would be to provide Narta with an authorisation for a more limited period, say 5 years. Narta is also open to conducting a review at the 3 year mark.

37) If Narta then found it necessary to seek reauthorisation it would be in the context of it being able to demonstrate that it had been able to access Exclusive Product and that this had resulted in the public benefits claimed. In Narta's submission it would be better outcome for competition for the Commission to allow Narta to compete on equivalent terms to all other participants in the wholesale electrical goods market, rather than to risk the significant and potentially irreversible reduction in both competition and consumer welfare that we submit will otherwise result.

Yours sincerely

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